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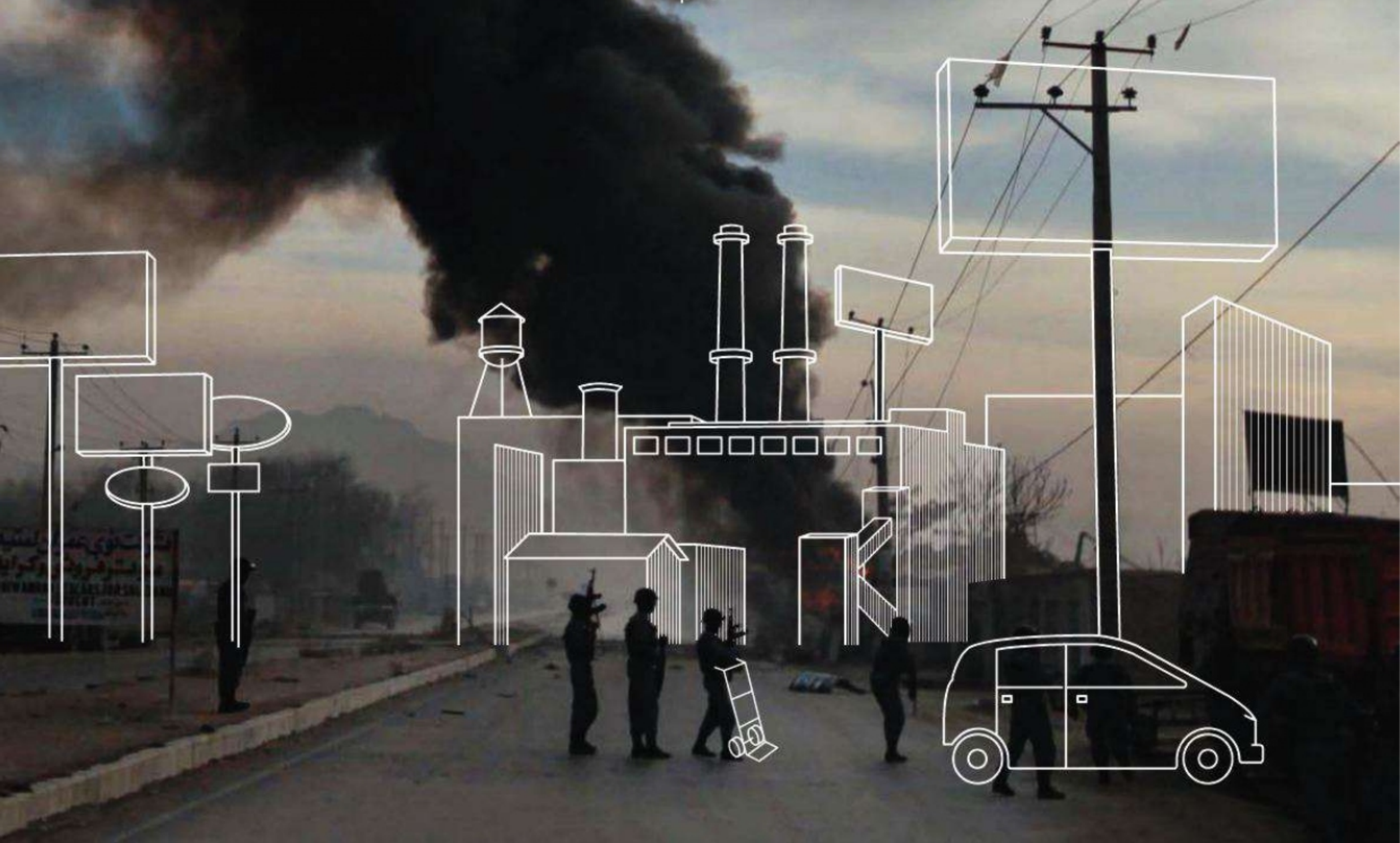
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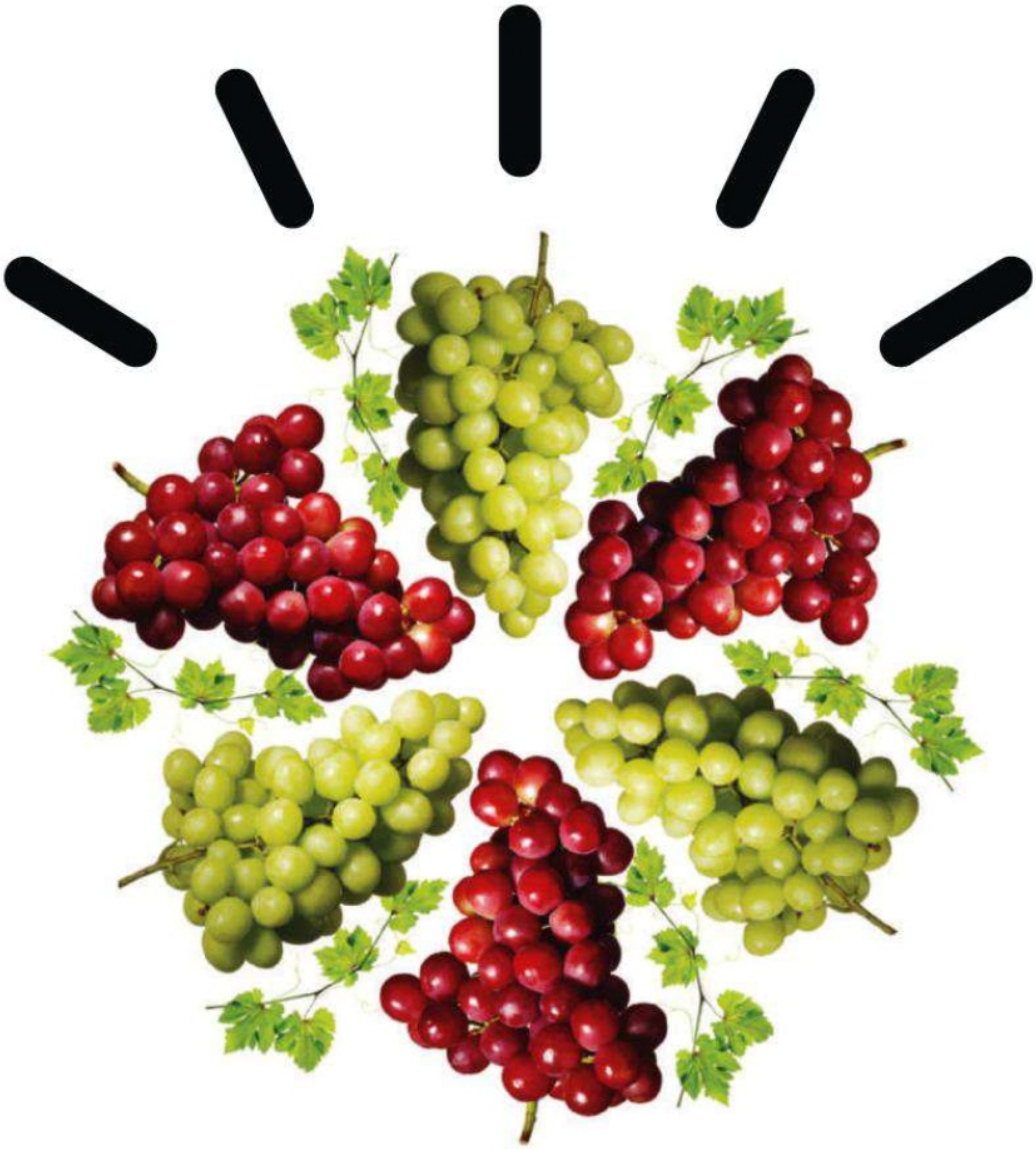
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Opening Remarks

Initial Private Offering

Facebook's new $450 million deal with Goldman Sachs is a triumph of antidemocratic investing. By Roben Farzad

As investors enjoy their second straight January with positive brokerage statements in the mail, there's more than a whiff of optimism in the air. The Dow Jones Industrial Average is on course for its biggest two-year bull run since 1932, and individual investors are finally showing signs of getting back into stocks. The period Dec. 1 to Dec. 29 saw a total of $14.90 billion move out of bond funds and $5.51 billion into stock funds.

The appetite for risk is back. For better or worse, people are ready to get in on the next hot play. America, after all, has always been a place where investors could ride the good fortunes of its most innovative companies. Hasn't it?

In 1995 the locus of innovation was Web pioneer Netscape Communications, whose initial public offering ignited five of the most lucrative years in market history. In 2004 it was Google, whose "Dutch auction" IPO invited anyone to bid on a share price; those who bid over $85–small and large investors alike–got in on what has turned out to be a 618 percent return.

Today, the It company is Facebook, the seven-year-old social network that last summer bagged its 500 millionth active user and whose founder and chief executive officer, Mark Zuckerberg, was named *Time*'s Person of the Year for 2010. When a privately held company displays this level of innovation and enjoys this level of success–when it captures the public imagination to such a remarkable degree–it's only natural that investors want to own a piece of it. Secondary exchanges such as SharesPost have been trading insiders' shares of Facebook at a level that values the enterprise at $42 billion. A Facebook IPO would benefit insiders and investors alike; all the 26-year-old Zuckerberg needs to do is reserve the ticker symbol–FACB? FRND?–and say the word, and the wealth-creating magic of democratic capitalism would unfold.

It isn't unfolding, however–at least for now. In what feels like a profoundly unfriendly move for a company with 500 million friends, Facebook has struck a private deal with Goldman Sachs and Russian investment firm Digital Sky Technologies (which is full of Goldman veterans) to sell them a $450 million and $50 million stake, respectively, in the company. A preferred and limited roster of Goldman clients would also buy in to the tune of about $1.5 billion. The deal, which values the social network at $50 billion, or more than two Yahoo!s, is expected to be structured by Goldman to allow Facebook to remain below the 500-investor threshold that would force it to make an array of Securities and Exchange Commission disclosures. A special Goldman fund with numerous client investors, the legal thinking goes, could be counted as a single investor.

Some funds within the wealth management division, such as the hedge fund Goldman Sachs Investment Partners, are also likely to get some of the private Facebook stock, according to two people familiar with the matter who requested anonymity because they weren't authorized to discuss the deal. Clients are being offered the opportunity to invest as much as $2 million apiece with Goldman taking a 4 percent placement fee and 5 percent of any investment profits plus an annual servicing fee, according to two clients who were offered shares. "If you're an underwriter, you love this kind of discretion," says Jay R. Ritter, a University of Florida professor who studies public offerings. "It gets you the maximum pay-to-play benefit."

America has always been a place where investors could ride the good fortunes of its most innovative companies

The structure of the deal is also novel. While Goldman Sachs routinely distributes offerings to its institutional and high-net-worth brokerage clients (minimum account size: $10 million), interested buyers this time would have to agree to hold on to their shares until 2013 and keep a lid on material nonpublic information. Stephen Cohen, a Goldman Sachs spokesman, declined to comment.

Laurie Simon Hodrick, a professor of capital markets at Columbia Business School, sees the arrangement simply as another venture capital round for a company that would rather remain private for now. Goldman, she notes, was willing to provide capital on the terms Zuckerberg wanted. "If Facebook is a student of history," she says, "they'll remember not just Netscape's IPO but the cautionary tale of what happened afterward." (After ceding its dominance of the browser market to Microsoft, Netscape sold itself off to AOL in 1999.)

Even so, this deal is a long way from the ideals of democratic capitalism. If anything, it signals that when Zuckerberg finally does decide to take Facebook public, the IPO will see value and information accrue to connected insiders, while those 500 million friends are left scrambling for aftermarket odd lots. Factor in the hot public offerings that have been limited to big investors recently–General Motors, Tesla Motors–and it's hard to argue that the resurgent IPO market, dormant for three years, is becoming more open.

It's a development that runs counter to the spirit, if not the letter, of the new financial regulations passed in the wake of the crisis. "The Facebook investment sends a message to institutional investors that Dodd-Frank and Basel III have not hobbled Goldman's business model and that the magic remains," says Brad Hintz, an analyst at Sanford C. Bernstein. "From Goldman's point of view, this is a way of ensuring it wins the lead underwriting position when Facebook goes public." That would not only generate a windfall on Goldman's current investment but

PHOTO ILLUSTRATION BY EMILY KEEGIN; BLANKFEIN: BLOOMBERG

Goldman CEO Lloyd Blankfein seems to like his own status



would also win fresh clients from Facebook's workforce and earn dibs on future IPOs from related plays like Zynga and Foursquare.

In truth, there has never been anything very public about the initial public offering. "The sad reality is that the only IPOs that the mom-and-pop investor have access to are the ones you don't want," says Rodd C. Langenhagen, a tech banker with Morgan Keegan. "Ironically, the more safeguards we build into the system to protect investors, the more companies don't want to go public, so investor access relies on even less regulated special purpose vehicles and secondary share markets. Just like drugs and alcohol, the more you regulate it, the more it's driven underground."

Brokerages that make their money by providing market access to small investors argue that the little guy is fully capable of giving issuers like Facebook the capital they need. "We want to provide a level playing field, equal access," says Paul Renken, vice-president of relationship management at E*Trade Financial. "There's a disconnect on Wall Street IPOs between shareholders and customers." He is among those who say that GM, the recipient of a $50 billion taxpayer bailout, slighted retail investors in its record November IPO by declining to allocate to online brokers. Aftermarket shares were the most traded on E*Trade that day, a signal of unmet retail demand. "It could have been a great opportunity for all involved," he says.

Facebook could be, too. For all the social network's fierce independence and little-guy appeal, however, Zuckerberg is apparently not bothered by the kind of insider capitalism that marked the dot-com boom and bust, a period that saw more than 300 lawsuits and settlements linked to IPO allocation fraud and compromised Wall Street research. But Facebook's founder was in high school then, and that tempest is long forgotten.

—With Christine Harper

Food: Freaky Weather, Scary Prices

▶ **A year of droughts and floods has pushed food prices up**

▶ **"Imperfect weather ... collided with perfect food demand"**

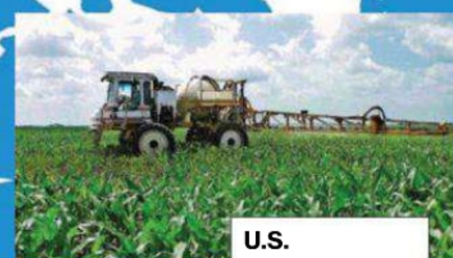
World food prices are back at levels last seen during the 2008 food crisis, when riots spurred bans on food exports in the most afflicted countries. The question now is whether the price surge of late 2010 will spill into 2011.

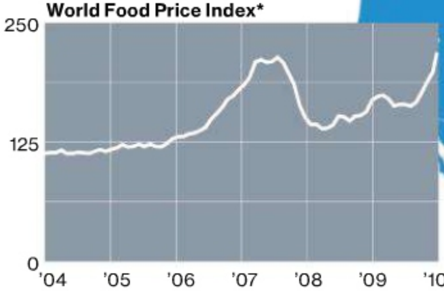
The U.N. Food and Agriculture Organization's index of world food prices rose 32 percent in the second half of 2010, topping the peak of June 2008. Low rainfall in Russia, Kazakhstan, Europe, and South America parched crops, while floods in Canada inundated them. China's growth spurred record demand for sugar and soybeans. Excessive rain in India has damaged the onion crop, driving the wholesale price of this staple up 40 percent in the 12 months ended Dec. 18. Developed countries' grain stocks–the reserves that keep consumption steady when harvests disappoint–will probably decline 25 percent in the 2010-11 crop year, according to the FAO.

And 2011? "We are coming out of a two-year period of relatively low food price inflation due to the recession," says Ephraim Leibtag, U.S. Agriculture Dept. food price forecaster. "Increased global trade coming out of the recession, some increased consumer demand, and higher energy and commodity costs for food production" will boost prices. The USDA expects a rise in oil prices to lift demand for ethanol by 5.1 percent in the U.S., which will affect corn prices. The agency foresees U.S. food inflation of 2 percent to 3 percent, the highest since 2008.

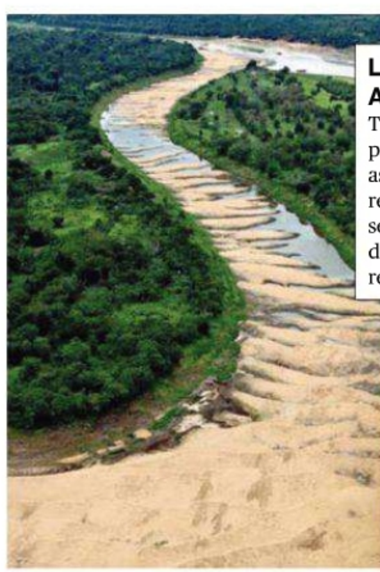
The rest of the world may feel pressure, too. Drought in Argentina and Brazil, the next biggest corn and soybean exporters after the U.S., and developing-world growth may push prices up further this year, says Gary Blumenthal, president and chief executive officer of World Perspectives, a Washington (D.C.) agricultural consultant. "Imperfect

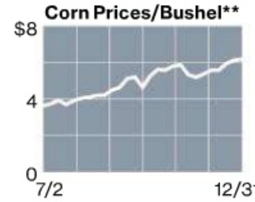






*Composite of prices of 55 food commodities





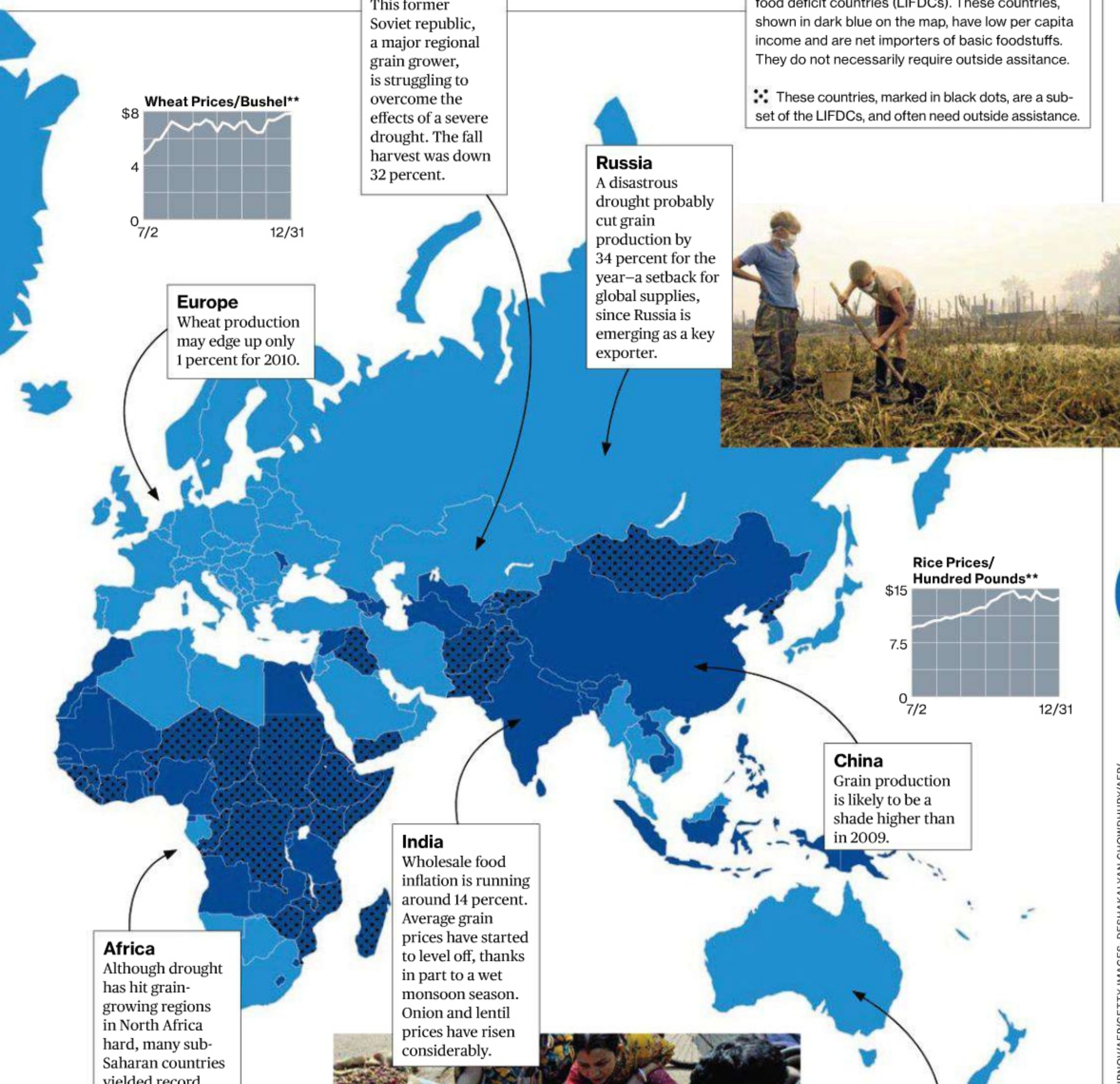
**Weekly quotes from Chicago Board of Trade

DATA: UN FOOD AND AGRICULTURE ORGANIZATION; CHICAGO BOARD OF TRADE; BLOOMBERG

worldmags

■ The U.N. categorizes 77 countries as low-income food deficit countries (LIFDCs). These countries, shown in dark blue on the map, have low per capita income and are net importers of basic foodstuffs. They do not necessarily require outside assitance.

⁙ These countries, marked in black dots, are a subset of the LIFDCs, and often need outside assistance.



Kazakhstan
This former Soviet republic, a major regional grain grower, is struggling to overcome the effects of a severe drought. The fall harvest was down 32 percent.

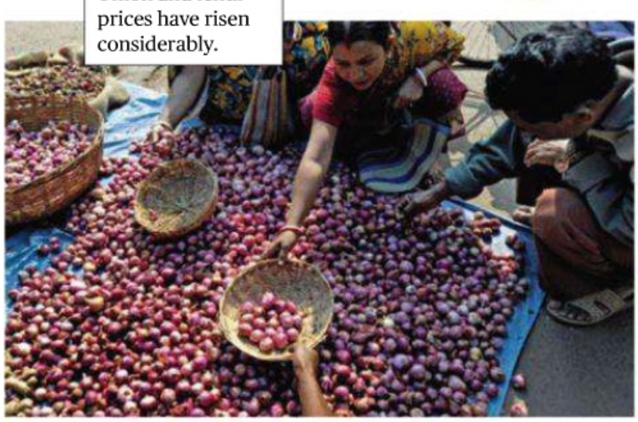
Russia
A disastrous drought probably cut grain production by 34 percent for the year—a setback for global supplies, since Russia is emerging as a key exporter.

Europe
Wheat production may edge up only 1 percent for 2010.

China
Grain production is likely to be a shade higher than in 2009.

India
Wholesale food inflation is running around 14 percent. Average grain prices have started to level off, thanks in part to a wet monsoon season. Onion and lentil prices have risen considerably.

Africa
Although drought has hit grain-growing regions in North Africa hard, many sub-Saharan countries yielded record harvests. Still, some 20 countries in Africa, including Zimbabwe, Kenya, Sierra Leone, and Congo, are in severe need of food assistance.



Australia
Ideal growing conditions in the East yielded a good crop. Recent floods in the Northeast may affect future output.

CLOCKWISE FROM TOP RIGHT: ANDREY SMIRNOV/AFP/GETTY IMAGES; DESHAKALYAN CHOWDHURY/AFP/GETTY IMAGES; RODRIGO BALEIA/LATINCONTENT/GETTY IMAGES; SETH PERLMAN/AP PHOTO

weather has collided with perfect food demand," he says.

The FAO does not see demand falling. "Consumers may have little choice but to pay higher prices," it says in its November price outlook. "With the pressure on world prices of most commodities not abating, the international community must remain vigilant against further supply shocks in 2011."

One good sign: "Many food-importing countries have improved their output," says Abdolreza Abbassian, senior economist for the FAO. Record crops were harvested in most countries of Eastern, Western, and Central Africa in 2010. Yet at the same time, the FAO identifies 20 African countries in crisis that still need outside food assistance. *—Alan Bjerga with Tushar Dhara*

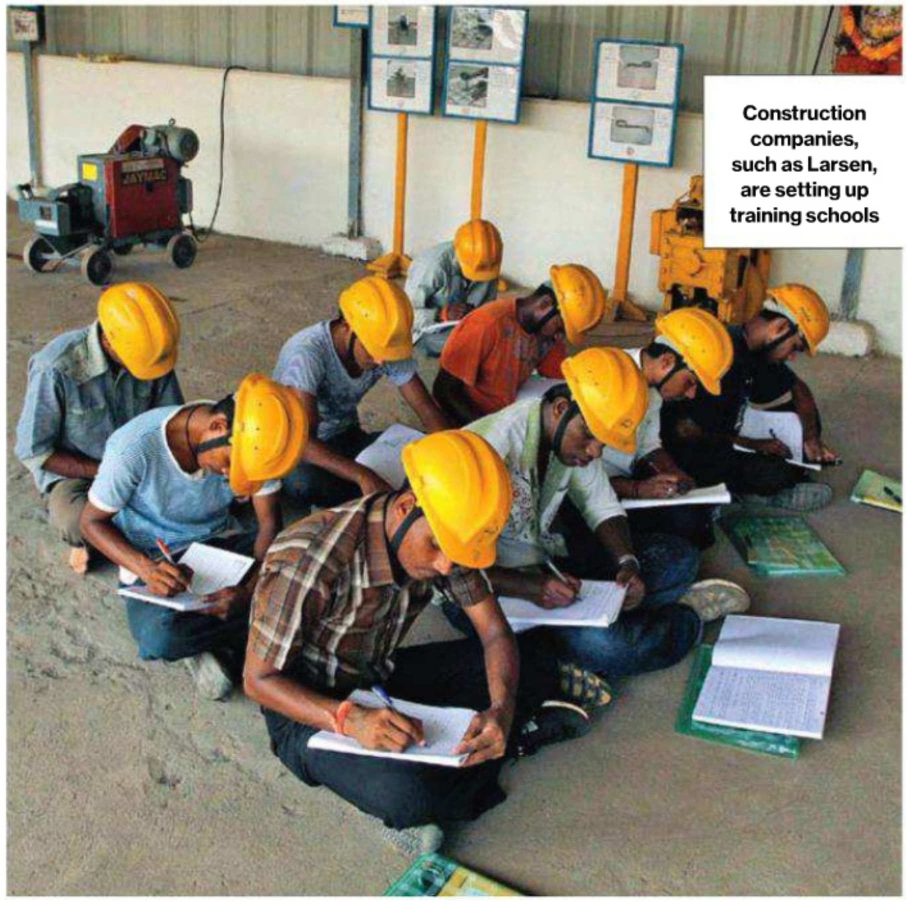
The bottom line *Food prices, especially for wheat and other grains, have surged back to 2008 levels. The coming year may see prices rise further.*

Infrastructure

Where Are India's Skilled Laborers?

▶ India is investing in infrastructure at last. Now it needs people to build it

▶ "If I was educated, maybe I could do his job"



Construction companies, such as Larsen, are setting up training schools

Vimla, 26, wipes the dust from her forehead with a faded blue sari and fills a round metal tray with broken stones that she carries, barefoot, across a building site for part of New Delhi's subway. "My job doesn't need any training," says Vimla, who uses only one name. Pointing to her supervisor, a man in a hard hat, she says: "I do what he says. If I was educated, maybe I could do his job."

Prime Minister Manmohan Singh has pronounced poor infrastructure the biggest impediment to India's growth. Yet India's roads, bridges, airports, and ports cannot be built without skilled labor. Builders including **Larsen & Toubro**, India's biggest engineering company, say that while the country has millions of unskilled workers like Vimla, it doesn't have enough masons, carpenters, and machine operators to construct the roads, railways, and ports the country needs. "Lack of skilled workers impacts on all three fronts: quality, delivery, and costs," says K.V. Rangaswami, president of construction at Mumbai-based Larsen.

India's economy was forecast to expand 9.7 percent last year, not far behind China's. Yet India is ranked 91st out of 139 nations for the quality of its infrastructure, behind Ethiopia and Indonesia, according to the World Economic Forum's *Global Competitiveness Report 2010-2011*. India's construction industry had about 31.5 million workers, 83 percent of them unskilled, in 2005, according to a report last year by the New Delhi-based National Skill Development Corp.

To help tackle the shortage, construction companies have set up their own training schools. Larsen runs one in Panvel, about 56 miles from Mumbai's financial center. On a recent day, Manoj Pehre was learning to bend steel rods into rectangles so they can reinforce concrete beams and columns.

Pehre, 23, says his family hopes the training will be a first step toward running his own contracting business. Around him, other men learn carpentry, bricklaying, and welding. The three-month apprenticeship costs Larsen 21,000 rupees ($467) per trainee. Virendra Mohod, 26, who's studying masonry, says the training will give them better pay, job security, and the chance to travel.

He and Pehre are among the lucky ones. Most workers are like Vimla, who moved to Delhi from Uttar Pradesh in northern India four years ago with her husband and her son Rinka. Her son clings to her waist as she carries that tray of rocks on her head, near the $275-a-night Taj Palace Hotel.

Plugging the skills gap will also require a cultural change, says A. Janakumar, a regional training manager at Larsen's institute in Panvel. Trades are traditionally passed down through families, and laborers don't get enough respect for their work, he says, since these jobs previously were done by underprivileged members of the community. "Fathers want sons to be engineers now, not carpenters," says Janakumar. *—Madelene Pearson and Malavika Sharma*

The bottom line *India lacks the carpenters, electricians, and construction equipment operators it needs to sustain growth.*

ADEEL HALIM/BLOOMBERG

Global Economics

U.S. Employment

Small Businesses Keep a Lid on Hiring

▶ They once led the way out of hard times. Now they do more with less

▶ "The recession definitely made me take a pause in ... wanting to hire"

Lee and Kate Amon, owners of Internet retailer **Kate's Caring Gifts**, say they would need a 50 percent increase in sales before adding a full-time employee. The couple, who live and work in Fremont, Calif., have two part-timers handle orders for organic food baskets and natural soaps because "it gives us the flexibility to add or subtract their hours," says Lee. "It costs us about the same to hire one full-time person. But if that person gets sick, we're toast."

As the U.S. economy gains momentum, small business employment is lagging behind other drivers of the recovery. Past rebounds were led by companies with fewer than 500 employees as they added full-time workers. Now some owners say they'll rely on part-time help and push their staffs to be more productive as they wait as much as a year for demand to improve. "I'm not sure we'll ever return to the type of full employment we've had in the past," says Charles W. McMillion, president and chief economist at forecasting firm MBG Information Services in Washington, who has studied labor markets for 30 years.

In the first 12 months following the recession that ended in November 2001, small businesses added 81,000 workers. After the most recent downturn, companies cut 480,000 during a comprable time period, according to data from ADP Employer Services. "Normally we look to small firms to account for a lot of the job growth," says Scott Brown, chief economist at Raymond James & Associates in St. Petersburg, Fla.

Instead, investors are "rewarding" the efficiencies that publicly traded small businesses adopted to battle the recession, says Michael Shaoul, chief executive officer of New York-based Oscar Gruss & Son, which provides research to institutional investors. Since Sept. 1 the **Wilshire Micro-Cap Exchange Traded Fund**, which includes companies with fewer than 500 workers and tracks shares of the Wilshire Index's 2,500 smallest stocks, has gained around 33 percent, vs. 19 percent for the Standard & Poor's 500 ETF Trust.

Small businesses "definitely have cut costs in terms of reducing workforces," says Joseph Kremer at Fifth Third Asset Management in Cleveland, who helps oversee $250 million in small- and micro-cap stocks. "That's good for their efficiency, but not necessarily good for the unemployment rate."

Underemployment was 17 percent in November. That includes people without jobs and those who gave up looking, as well as those who work part-time but want full-time jobs. Many of the latter are "in trouble in terms of paying the bills" even though they are "still going to work," says Dean Baker, co-director of the Center for Economic and Policy Research in Washington.

Josh Frey, chief executive officer of **On Sale Promos** in Washington, fired six of seven full-time salespeople in 2008. When he offered to keep the employees on as contractors, all accepted, he says. Since then, Frey has cut costs on benefits, payroll taxes, trash removal, electric bills, and an office lease for his business, which puts corporate logos on T-shirts, mugs, and pens. "The recession definitely made me take a pause in terms of wanting to hire," says Frey, 39. He's unlikely to add full-time workers even after business improves because, he says, "I've never been more profitable." *—Vivien Lou Chen and Timothy R. Homan*

The bottom line *Small businesses are figuring out how to increase efficiencies and boost margins without hiring more full-time workers.*

0.7

PERCENT

Increase in U.S. factory orders for November. The median forecast of economists surveyed by Bloomberg News called for a 0.1 percent drop. The gain signals that the recovery in manufacturing may gain momentum.

DATA: U.S. COMMERCE DEPT., BLOOMBERG

Natural Resources

Rare Earths from Japan's Junk Pile



KIYOSHI OTA/BLOOMBERG

▶ It's mining discarded appliances as China slashes supplies

▶ "We need a stable supply, and recycling is a part of that"

It takes two **Hitachi** workers eight minutes to slice open the metal casing of a used air conditioner compressor. The prize inside: four wafer-thin magnets containing about 30 grams of rare earth metals.

Hitachi, which makes everything from nuclear power plants to home appliances and batteries, uses as much as 600 tons of rare earth metals in its products each year. It is one of hundreds of Japanese manufacturers depending on rare earth shipments from China, which produces 97 percent of the world's supply of the lightweight, malleable metals essential to hybrid cars, cell phones, and hard disk drives.

In the second half of last year, China cut its exports of rare earths by as much as 72 percent. Then in late December, the Chinese government said it would restrict shipments again in 2011 to free

Global Economics



Tadashi Yanai's fashion faux pas page 16 ▶

up supply for local manufacturers and rein in an industry that is damaging the environment with waste gas, heavy metals, and other pollutants.

The export clampdown has driven up prices and sent Japanese companies, the world's biggest users of rare earths, scrambling to find other sources. "Japan imports nearly all its metals, but the difference with rare earths is that they are used for environmental technology and high-efficiency motors, which is where the market is now," says Hikaru Hiranuma, an analyst with Tokyo Foundation, a research center based in Japan's capital.

Hitachi says it expects recycling to meet 10 percent of its rare earth needs by 2013, up from almost zero now. "We need to make sure we have a stable supply, and recycling is part of that," says Kenji Baba, general manager of Hitachi's resource recycling office.

Inside a warehouse in Matsudo City, Hitachi demonstrated the results of its recycling research one day in December. Four refrigerator-size devices used saws to open up compressors without damaging the rare earth magnets inside. A separate conveyor belt fed disk drives into a machine about the size of a ship container. The drives came out the other end in pieces ready for rare earth harvesting. Hitachi says the machines are the first of their kind.

The drop in exports from China, combined with rising demand from Hitachi and other companies, drove the price of neodymium, one of the rare earths, to a recent $88.50 a kilogram from $19.12 in early 2009, according to **Lynas**, a rare earth miner based in Sydney. Lynas is building a $535 million rare earths mine in Western Australia. Neodymium is used in the batteries that help power the **Toyota** Prius.

"China's monopoly isn't going to hold up because prices are high enough now to make it worthwhile for other people to get into the business," says Mitsushige Akino, who oversees about $450 million in assets at Tokyo-based **Ichiyoshi Investment Management**. Trading company **Sojitz**, one of Japan's biggest importers of rare earths, has agreed to buy as much as 9,000 tons annually from Lynas' Mount Weld mine over the next 10 years. **Sumitomo**, Japan's No. 3 trading company, says it's considering an investment in Colorado-based rare earth miner **Molycorp.**

Other Japanese companies are following Hitachi's lead and mining discarded products. Tokyo-based chemical maker **Showa Denko** has opened a plant in Vietnam to begin recycling dysprosium and didymium, rare earth metals used to strengthen magnets. The company, a top producer of components in hard disk drives, plans to recycle 800 tons of rare earth metals at the factory. Copper processor **Mitsubishi Materials** has recycling joint ventures with **Panasonic** and **Sharp**. It has also started researching the cost of extracting neodymium and dysprosium from washing machines and air conditioners. *—Jason Clenfield, Mariko Yasu, and Stuart Biggs*

The bottom line *China's decision to restrict exports of rare earth metals has prompted Japanese companies to find new sources of supply.*

Euro Zone

Joining the Euro: What's the Hurry?



▶ **Poles and Czechs are better off for now without monetary union**

▶ **"In the end they will join the euro, but this [will] be a longer process"**

Just a year ago, Poland and the Czech Republic were proceeding with plans to ditch their currencies, the zloty and the koruna, and join the euro zone. By doing so, they would benefit from the usually favorable interest rate policies of the European Central Bank and solidify relations with their biggest trading partners. Euro membership would cap off a 20-year transformation from outlier states in the Soviet empire to thriving workshops for Western Europe.

Now—surprise!—the Poles and Czechs are getting cold feet as the euro zone staggers

➜ 14

Tom Keene's EconoChat

Tom talks with **Jon Shure,** deputy director of the State Fiscal Project at the Center on Budget and Policy Priorities

Some folks think the states' fiscal situation is not as dire as many think because tax receipts are coming back. Do you agree?
Revenues have just started to pick up a little. But the big problem is that in the last two years the states were helped a lot by money from the Federal Recovery Act, and that money is just about gone now. So even with a tiny uptick in revenue, the hole is getting bigger.

There's story after story about states cracking down on unions and cutting salaries. Is this the right strategy?
States are in a huge hole because they have never seen a drop in revenues like they saw during this recession. If the states' finances were in perfect shape, they would still be in a huge hole because of this drop in revenues. We always need to spend efficiently, but there are some folks who don't like the fact that public workers get decent benefits when people in the private sector no longer do. And instead of making people in the private sector more economically secure, they want to take it away from somebody else.

When you say that there needs to be spending responsibility, how do you envision that?
One area where spending has grown tremendously is the tax breaks given to businesses in the hopes they will create jobs. Yet the states never go back to evaluate the tax breaks to find out if we got what we paid for. Is this a better use of money than investing in education and transportation?



Keene hosts Bloomberg Surveillance *7-10 a.m., 1130AM in New York, XM 129, Sirius 130.*

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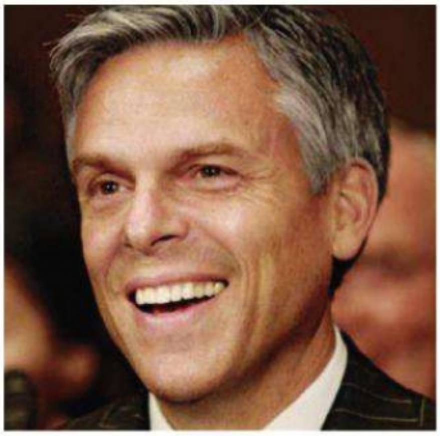
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Charlie Rose talks to

Jon Huntsman



The U.S. Ambassador to China–and long-shot Republican contender for President–talks about how and why decisions are made in Beijing

You're a man often mentioned as having a very bright political future. So President Obama comes to you and says: "I want you to be my ambassador to China." Why? And why did you say yes?
I like to think he did it because he cares about the relationship in the sense that bipartisan management matters. In 31 years of our diplomatic relationship, it hasn't given away to political extremes. It's been managed in a bipartisan fashion. And I accepted it because the President asked. If you can make a unique contribution, hardship though it might be, you stand up and serve.

Talk about the fear that China is expanding its military.
Of course they're expanding. They have the money to expand. We welcome their rise, so long as it is in keeping with standard rules of the road.

Is it your sense that they want to become a sea power?
They're building big ships. And they're very sophisticated ships. Their hardware is getting quite good, very advanced and sophisticated. And they have, of course, regional interests.

What are those interests?
If you get right down to the core interests, it's preserving the Communist Party. And how do you preserve the party? By delivering economic growth that is 8, 9, 10 percent per year, which they've been able to do for 30 years. So I would argue that first and foremost, they want a stable region ... an environment in which one can grow their economy. That's, I think, Job One.

Their dominant position in rare earth metals has become a flash point.
What will ameliorate this problem somewhat is the fact that many countries in the world are bringing online, in 2012, greater production of rare earth products. The U.S. has plenty of rare earth products. It's [a question of] economic cost and environmental cost. How badly do you want your own indigenous supply of these products? All we're asking for is that [China] not use rare earth products as a trade weapon. They had a tussle recently with Japan over a fishing vessel. It could be argued that in fact it was used as a trade weapon. [China cut off rare earth shipments to Japan for two months last year.]

Is there now a sense that China recognizes its economic heft?
I think there is clearly evidence that they've been empowered with their newfound economic strength–[they're] now the second-largest economy in the world. They are about one-third of our own in terms of GDP, $5 trillion vs. $15 trillion. What we don't sometimes focus enough on when we look at and analyze China is their domestic challenges. So yes, they're growing, there's no question about that. But they're also transitioning 800 million farmers into a world in which they only need 200 million farmers. So what do you do ... ? You boost the economy. You put $600 billion in stimulus spending into the economy.

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What do you see happening with the U.S.-China exchange rate?
They're beginning [to revalue] once again ... and you see a very gradual appreciation, I mean painfully slow, and I'm guessing that they're doing it not just because the U.S. and Europe and others are saying it's important to us from a trading standpoint to have a currency that is properly valued. They're doing it because they see it's in their immediate interest. Inflation is on the horizon. They're trying to transition from the largest export power ever assembled in the history of the world to a consumer-based model. In order to do that you've got to have a properly valued currency. They've got to convince their citizens that now's the time to take renminbi out from under the mattress.

Will we be able to compete for this rise in consumer demand?
I think without question.

So it's a plus for the U.S.?
Without question.

When does China's political system finally evolve?
You'll have Xi Jinping rise to the top in 2012, and Li Keqiang will likely become the Premier. The stakes are enormously high. There'll be a level of ideological rigidity between now and the turnover ... because you've got to wear the straitjacket in the runup to those leadership changes, and then you consolidate your power base, which may take you to 2013. Then you've got a few years in which you can actually engage in change and reform. I would say the years 2013 to 2015, 2016 are going to be pretty important from a reform standpoint. B



Watch Charlie Rose on Bloomberg TV weeknights at 8 p.m. and 10 p.m.

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into the new year. Czech central bank board member Robert Holman says setting a date for euro adoption "would be very risky and unwise." Polish central bank President Marek Belka wants the euro zone to "normalize" before his country joins. By pausing in their march to the euro, Poland and the Czech Republic can hold on to their currencies, which have been relatively stable. Their independent central banks can also defend their economies in case of a market upheaval, instead of relying on the embattled ECB.

Not everyone in Eastern Europe is shying away from the euro: Tiny Estonia joined the zone on Jan. 1. Yet its gross domestic product of $19 billion is puny compared with the combined $631 billion GDP of Poland and the Czech Republic, which have built up successful auto, IT, and general manufacturing industries.

Analysts like Ulrich Leuchtmann understand why the Poles and Czechs hit the hold button. "A couple of years ago this would have been negative" for the koruna and zloty, says Leuchtmann, the head of currency strategy at Frankfurt-based Commerzbank. Now, stalling on the euro is "net positive," because the financial health of Poland and the Czech Republic is better than such euro zone weakling states as Greece and Ireland, he says. The Czech economy is forecast to grow 2.3 percent this year while Poland's may expand 3.9 percent, compared with 1.5 percent in the euro region, according to the European Commission.

The Czechs plan to push through austerity measures, which, combined with low inflation, may cut their borrowing costs to below Germany's by 2012, according to forecasts from BNP Paribas. The Czech budget deficit was an estimated 5.2 percent of GDP in 2010; by comparison, Greece's was 9.6 percent. "The East European countries clearly see the benefits of having a flexible currency right now," says Thomas Kirchmair, who helps manage 12 billion euros ($16 billion) in European bonds at Deka Investment in Frankfurt. "In the end they will join, but this is going to be a longer process." Ⓑ

—Jason Webb, Peter Laca, Krystof Chamonikolas, and Piotr Skolimowski

The bottom line *The Poles and Czechs have decided to bide their time before joining the euro. Both benefit from keeping their own currencies.*

Seven Days

Events of note in the week ahead

by Ira Boudway

10

Alcoa earnings

▶ **North American International Auto Show:** The annual industry gathering in Detroit opens for a press preview.

▶ **BCS National Championship Game:** The Oregon Ducks and Auburn (Ala.) Tigers meet in Glendale, Ariz.



11

Japan's trade balance for November

Bank of Italy lending and bad debt data for November

▶ **Oil spill report:** The National Commission on the BP Deepwater Horizon Oil Spill, co-chaired by former Democratic Senator Bob Graham (Fla.) and ex-EPA head William K. Reilly, delivers its final report.



12

Fed *Beige Book* released

Germany's GDP for 2010

▶ **NAHB International Builders' Show:** Some 1,200 housing and construction companies open booths for an expected 60,000 visitors in Orlando.

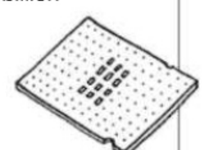


13

China's Leading Economic Index

European Central Bank announces interest rate

▶ **Intel earnings:** Analysts expect revenues of nearly $11.4 billion for the chipmaker, up from $10.6 billion in the same quarter last year.



14

The Republican National Committee elects a chair

JPMorgan Chase earnings

▶ **Berlusconi ruling:** After delaying in December, Italy's Constitutional Court is scheduled to rule on Prime Minister Silvio Berlusconi's temporary immunity from prosecution.



15

NFL playoff divisonal round begins

▶ **Wikipedia's 10th birthday:** The online encyclopedia celebrates, in typically decentralized fashion, with dozens of events around the world (page 57).



16

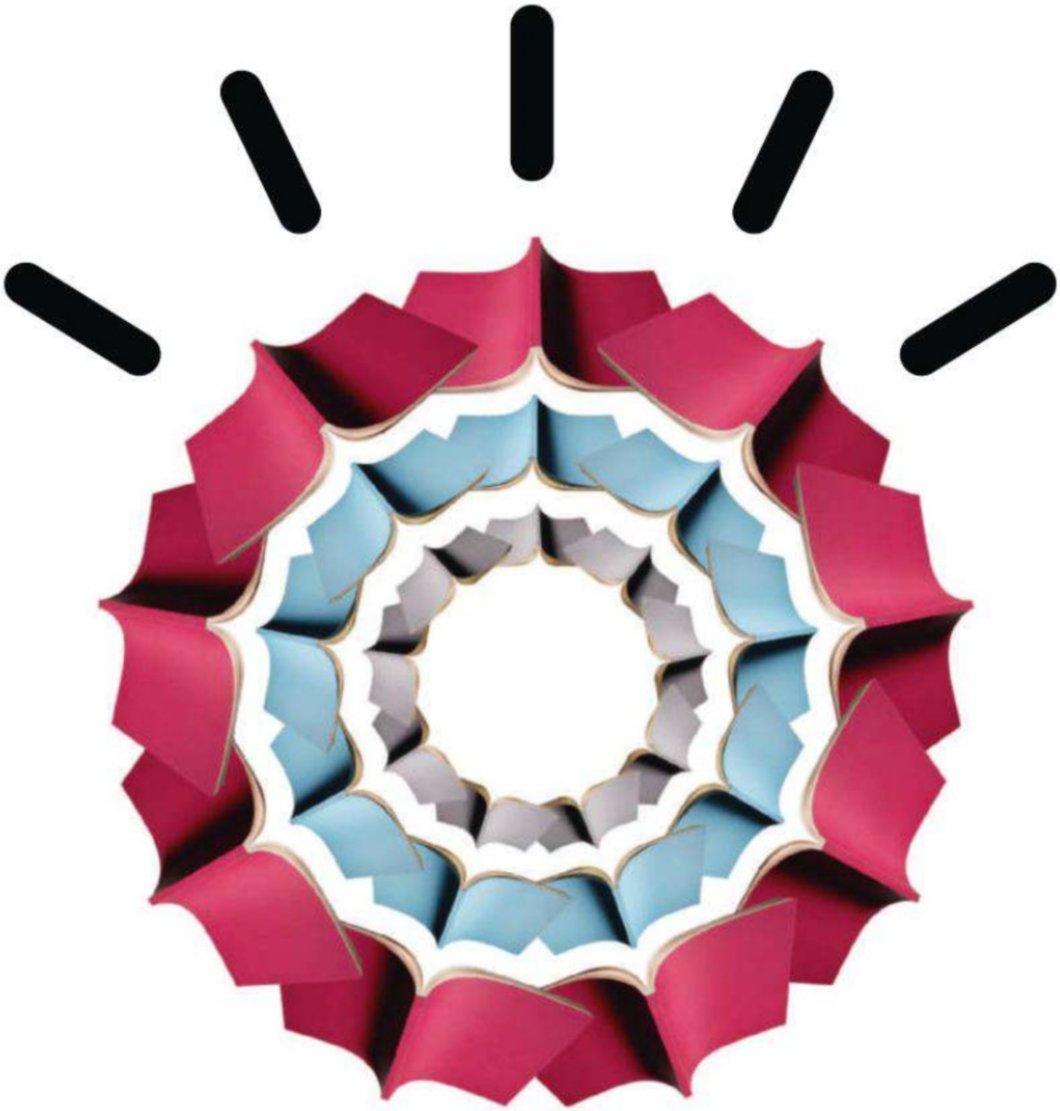
Winter Fancy Food Show in San Francisco

▶ **Presidential runoff in Haiti:** Mirlande Manigat is scheduled to face either René Préval's favorite, Jude Célestin, or musician Michel Martelly, depending on the outcome of their dispute over second place in the Nov. 28 vote.



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Asia's Top Clothier Is Back to Basics

▶ **Tadashi Yanai, Japan's richest man, hits a bump at Uniqlo**

▶ **"The company tilted to fashion items that didn't sell"**

Tadashi Yanai, founder and president of **Fast Retailing**, built his roughly $9.2 billion fortune by turning his father's tailor shops into Uniqlo, the chain of low-priced casual wear stores that is Asia's largest clothing retailer. Yanai has doubled Fast Retailing's sales in the past five years and wants to increase revenue sixfold, to 5 trillion yen ($60 billion), mainly by quadrupling the number of Uniqlo stores worldwide, to 4,000 by 2020. Last year, however, things went terribly wrong. The decision to produce numerous styles of fashionable clothing—never Uniqlo's strength—left it with plenty of slow sellers in the spring. The situation worsened in the fall and winter, as its stores failed to stock enough basic items, like its popular New Ultra Light Down gear.

To top things off, growing competition in the Japanese market—home to 826 of Fast Retailing's 975 stores and the source of 80 percent of its annual sales—is forcing Uniqlo to offer discounts to hold on to customers. One result of these challenges: Revenue at stores open more than a year fell 25 percent in September and continued to slide through November. The company already is forecasting its first profit decline in four years for the fiscal year ending next August. Spooked investors sent Fast Retailing's shares plunging 26 percent in 2010. "Fast Retailing lost focus on its core products," says Mikihiko Yamato, an analyst at Japaninvest in Tokyo. "The company tilted to fashion items that didn't sell well."

Uniqlo is increasingly bumping heads against other apparel retailers hungry for international growth, including the Zara brand from Spain's **Inditex** and the H&M stores unit of Sweden's **Hennes & Mauritz**. Both chains, which offer low-priced clothing pegged to the latest fashion trends, have invaded Uniqlo's backyard. Zara opened its first store in Japan in 1998 and now has 63 outlets there. H&M has added 10 stores since entering Japan in 2008. And both have established much larger beachheads in the U.S., where Uniqlo has just one store in New York's trendy SoHo shopping district.

Uniqlo's big international push lies ahead. Meanwhile, both Zara and H&M have invaded Japan

Analysts and investors worry that trying to match the European interlopers at home took Uniqlo off track. "The company followed trendy makers like Zara," said Yamato of Japaninvest. "Uniqlo needs some fashion items, but the company's strength is to mass-purchase fabrics to make large quantities of functional clothing." Adds Koichi Ogawa, chief portfolio manager at Daiwa SB Investments: "The company should stick with its basic designs to differentiate itself from Zara and H&M."

Yanai has gotten the message. "We were driven by 'surface fashion' too much," he told reporters in October, referring to products that he said have "a meaningless design such as a shirt with a frill attached in a meaningless part." Yanai declined to be interviewed for this story. Going forward, he said, "we will strengthen our basic lines," like denim and Uniqlo's popular lightweight Heattech apparel, whose fibers are engineered to absorb and retain heat. The company forecasts Heattech sales will grow 40 percent, to 70 million items, this fiscal year. To make that happen, Yanai has reassigned top executives well-versed in basic—rather than fashion—clothing from other Fast Retailing apparel units to run merchandising at the flagship Uniqlo chain. (Fast Re-



Yanai, in a Paris Uniqlo store, plans to avoid "meaningless design"

CAPMAN/SIPA PRESS


Slim Fit Straight
T-000 Skinny Fit
S-002 Regular Fit Straight
S-001 Slim Fit Straight
A 9.90EUR
A 9.90EUR

tailing also owns the Theory and Comptoir des Cotonniers fashion lines, lower-priced apparel operations in Japan, and a French lingerie brand.)

Outside Japan, Uniqlo operates 149 stores in China, Britain, France, Singapore, Russia, Taiwan, Malaysia, and South Korea, plus its lone U.S. outlet. Yanai says he'll grow by opening more foreign stores, especially across China and fast-growing Southeast Asia. In the U.S., Uniqlo plans to open at least 200 stores by 2020, says Shin Odake, chief executive of its U.S. unit. The chain will hire 50 U.S. college graduates this year and send them to Japan for six months of training to become managers, he says.

Analysts say Fast Retailing is wise to target global growth, given its huge exposure at home. "Yanai should keep pursuing expansion abroad, as Japan is shrinking and offers little growth," says Daiwa SB Investments' Ogawa.

—Naoko Fujimura and Shunichi Ozasa

The bottom line *Japan's Fast Retailing stumbled in a move into fashion at its Uniqlo chain. Billionaire CEO Yanai is moving back to simpler clothing.*

17

PERCENT

Increase in global television shipments in 2010. In North America, however, shipments likely rose less than 1%.

DATA: NPD GROUP, DISPLAYSEARCH



Education

For-Profit College Grads Also Earn a Life of Debt

- **The schools leave students more indebted than conventional colleges**
- **"I got a ... student loan, no job, and I'm further and further in debt"**

Ronnie Franklin borrowed to pay his tuition at a for-profit college that advertised its success in preparing graduates for better jobs. The decision still haunts him. Despite graduating from RETS Technical Center in Boston in 2000, he found himself so strapped for money that he and his two sons lived in a homeless shelter last year. Frustrated that his degree didn't lead to work in electronics, Franklin—now a $12-an-hour housepainter—decided to go to a community college this year. He can't qualify for a federal grant that would pay the cost because he has defaulted on $20,000 of his earlier U.S. student loans.

Students seeking to move up in life by getting a degree from a for-profit college are being trapped in a growing underclass of education debtors. Under U.S. law, their loan obligations can rarely be discharged in bankruptcy, making them more onerous than credit-card debt or subprime mortgages. Defaults can subject students to government confiscation of salaries, tax refunds, and Social Security payments—and disqualify them for aid to get more marketable degrees.

Students at for-profit colleges carry the biggest loans in U.S. higher education. Bachelor's degree recipients at for-profits have median debt of $31,190 compared with $17,040 at private, nonprofit institutions and $7,960 at public colleges, according to Washington-based nonprofit Education Trust.

While currently enrolling one in eight U.S. students, for-profit colleges account for almost one in two federal-loan defaults. The Obama Administration wants to curb rising default rates and the threat of student destitution by cutting off federal funds to for-profit college programs whose students have the worst loan-repayment rates and lowest incomes relative to debt, which suggests their degrees aren't translating into higher salaries. That's if a degree is earned: The graduation rate for first-time, full-time candidates for four-year degrees at for-profit colleges is 22 percent, compared with 55 percent at state colleges.

For-profit colleges have higher student-loan default rates and dropout rates because they serve lower-income students, minorities, immigrants, and working adults, says Harris Miller, president of the Association of Private Sector Colleges and Universities, a trade group.

Don Harris, president of RETS at the time Franklin attended, says 80 percent of RETS graduates succeeded in finding jobs related to their fields within 60 days of graduating. **Washington Post**'s Kaplan Higher Education bought RETS in 2002. About 20 percent of students at the school, now called Kaplan Career Institute, default in the first two years they're required to make

CLOCKWISE FROM TOP: RICHARD DRURY/GETTY IMAGES; BRUCE GLIKAS/GETTY IMAGES; ILLUSTRATION BY TOPOS GRAPHICS

"Shovel-ready" snafus
page 28 ▶



payments—more than three times the rate at public colleges. That figure reflects the low-income backgrounds of Kaplan students, spokeswoman Melissa Mack says. "Most Americans are willing to take some risk with a student loan, knowing the payoff for them individually can be quite significant," Miller says.

The degree didn't pay off for Franklin. "I got an outstanding student loan, I got no job, and I'm further and further in debt," he says. "It's basically crippling me from doing a lot of things to improve my living condition." —*John Hechinger*

The bottom line *Students at for-profit colleges graduate with higher debt loads and loan default rates than those who attend conventional schools.*

Dieting

Nutrisystem Gets Real With Its Diet Ads

▶ **The weight-loss company recruits ordinary folks for its TV spots**

▶ **Before the diet plan, "I could not get on my horse by myself"**

For decades, **Nutrisystem** has used celebrity endorsers from the entertainment and sports worlds to pitch its weight-control foods to Americans anxious to drop a few pounds after holiday overindulging. Not this year. As Nutrisystem heads into the diet industry's most lucrative season, the maker of prepackaged, low-calorie meals is giving endorsers such as Marie Osmond and football great Dan Marino a lower profile and using testimonials from customers instead. "These are real people. We want them to inspire others," says Chief Executive Officer Joe Redling about the several dozen customers featured in a series of commercials that began rolling out on Dec. 26.

The switch in marketing strategy comes as Nutrisystem, based in Fort Washington, Pa., tries to catch up to rivals. While both Nutrisystem and **Weight Watchers International** lost customers during the recession, Nutrisystem continues to lag even as the economy begins to improve. According to company reports, Weight Watchers boosted third-quarter sales by 1.9 percent; Nutrisystem sales fell 4.1 percent, and the number of new customers it attracted declined by 10 percent. Since Redling took the helm in 2007, annual revenue has slumped 32 percent, and in 2010, Nutrisystem shares fell 32 percent. "They've had a tougher time getting people to sign up," says Wedbush Securities analyst Kurt Frederick. "Trying something different is a good idea."

The new campaign marks the first time in Nutrisystem's 38-year history that it has not primarily used celebrities to pitch its meals, which are priced at $299 for a month's supply. In September, the company began seeking first-person diet anecdotes by mailing hundreds of **Cisco Systems**' Flip video cameras to clients. As for the videos they got back, says Redling, "they were real, they were heartfelt [and] sincere."

Charlotte Husser, 54, is one of several dozen customers featured in the TV commercials. "What you're hearing from me has to come from the heart; there's no script," says Husser, who says she shed 32 pounds to become a size six after eating Nutrisystem meals for five months.

While Redling says his company will continue to use Osmond and Marino, celebrity endorsers are risky, says Bob Dorfman, executive creative director at Baker Street Advertising in San Francisco. "Advertisers have to be a lot more cautious about using celebrities" because their appearance and personal lives are increasingly dissected in the tabloids and on TV, he says. "It's important that they look good 100 percent of the time."



Osmond is on hiatus as Nutrisystem showcases real customers

Marino, a quarterback for the Miami Dolphins from 1983 to 1999 and now a sports commentator for **CBS**, says he's all for using real people: "Nutrisystem wants to convey how they're helping people lose weight and how it's affecting the lives of people that are noncelebrities." Osmond, who starred on the *Donny & Marie* TV show in the 1970s, declined to comment.

The Campaign for Real Beauty used by **Unilever** to promote its Dove soap is the classic case of using reg- ➜

Speed Dial
Scott Flanders

The Playboy Enterprises chief executive talks about the brand's prospects in Asia—and founder Hugh Hefner's bid to take the company private

You've just opened a Playboy Club in Macao, China's gaming hub. How does this fit into your Asian plans?
The major focus of our growth is going to be licensing and our club business. Five years from now, 90 percent of our profits will come from licensing and clubs. Asia will account for 30, maybe 40, percent of that 90 percent.

But Asian governments restrict adult entertainment.
Asia [is] the region where we have the lightest footprint from a media standpoint, yet it is our strongest licensing market. Playboy is a fashion brand in Asia, more than anywhere else. That's the magic of the brand Hef built. He always was an advocate for women and how men should treat women and how men can be attractive to women.

China's government often campaigns against pornography. How do you overcome that?
China is the single biggest country for us in terms of licensing. We're not launching any media properties in China; we are licensing our brand image to go on relevant products: accessories, jewelry, handbags. We have been in business in China for over 20 years and haven't had any issue.

What can you say about Hugh Hefner's proposed buyout?
Hef believes the company's best days were when it was private. He would like to return to that status. The board has a special committee evaluating his proposal. Hef owns 70 percent of the voting control; he has no fiduciary duty to sell to anyone. So when he says he is a buyer and not a seller, that speaks for itself. Ⓑ —*Bruce Einhorn*

ular folk in ads, says Kevin Lane Keller, a marketing professor at Dartmouth College. Dove's marketing blitz, which began in 2004 and has featured women from age 20 to 95, aims to boost the self esteem of girls by showcasing real people instead of models. Although the company won't provide numbers, Unilever spokesman David Perez says "response to our campaigns featuring real women has been overwhelmingly positive."

Keller says movie stars "may not seem as personally relevant because people don't see themselves as celebrities. That's when you'll bring in someone like a Jared," he says, referring to **Subway** sandwich chain spokesman Jared Fogle, who lost 245 pounds eating the restaurants' turkey and veggie subs.

Husser says Nutrisystem probably chose her for its campaign because the video she submitted showed her climbing onto her horse, nicknamed Edge. Before the diet plan, "I could not get on my horse by myself. Now, of course, I just hop right up there," says Husser, of Hammond, La. "That's pretty cool."

Nutrisystem's rivals continue to flaunt famous faces during New Year's resolution season. Actresses Valerie Bertinelli and Sara Rue appear in commercials and blog about dieting for **Jenny Craig**, owned by **Nestlé**. And Weight Watchers' website features a slimmed-down Jennifer Hudson, the actress and singer who found fame on TV's *American Idol*. Visitors can read about Hudson's seven-day meal plan. The Academy Award winner shared her Weight Watchers success story with millions of viewers before performing a new song on Dec. 31 on ABC's *Dick Clark's New Year's Rockin' Eve 2011*. Weight Watchers spokeswoman Nisha Chhabra says the appearance was a paid promotion and the song's lyrics contain Weight Watchers current tag line, "It's a new day."

Expect plenty more such testimonials in the coming weeks, a time when many consumers traditionally vow to reverse holiday weight gain. For weight-loss companies, explains Janney Montgomery Scott analyst Mitchell Pinheiro, "it's all about being on television and in front of customers in the first quarter, especially in January." —*Leslie Patton*

The bottom line *Struggling Nutrisystem is using real customers, rather than celebrities, in commercials airing during the peak post-holiday season.*



Von Sperling, right, puts a finishing touch on a client in Manhattan

Personal Services

A Makeover for Image Consultants

- **As the economy tanked, so did the market for personal shopping**
- **During the boom, styling the rich was akin to "living like a rock star"**

The Great Recession scorched many a lucrative, bubble-era vocation: Realtor, yacht broker, starchitect. Add to that list the image consultant. **Tiffany** and **Coach** are selling bling again, yet wealthy folks are more inclined to pick it out themselves than pay Samantha von Sperling $300 an hour to help them dress for excess.

Two years ago von Sperling, a New York image consultant whose previous careers include makeup artist and actress, was teaching the nouveau riche the art of conversation, and leading executives and their spouses on six-figure shopping trips through Manhattan boutiques and department stores. Today, revenue at von Sperling's Polished Social Image Consultants has fallen by about half; clients call less often or ask for deals.

Image consulting, of which personal shopping is an integral part, has been around since the '80s, when it became fashionable to have one's colors analyzed. In the mid-2000s, rising home and stock values made dropping thousands on makeovers seem almost appropriate for even the merely affluent. Reality shows like *What Not to Wear* and *Queer Eye for the Straight Guy* also encouraged regular folks, including men, to look for styling help. In 2008, "we were on the crest of a wave with all the TV programs," says Lynne Marks, founder of the London Image Institute, a school for would-be consultants in Atlanta. "Everybody knew what an image consultant was because we were everywhere."

Most image consultants charge an hourly fee from $50 to $300 or more for services ranging from how to work a room to matching ties with dress shirts. They often hail from the retail or beauty industries, and some pay upwards of $10,000 for training at schools that have opened in recent years.

During the boom, von Sperling's clients took personal shopping to new extremes. She recalls a female banker

Quoted

"What we've done over the years, quite successfully, is what we called the intelligent misuse of aircraft."
—Tony Tyler, CEO, Cathay Pacific Airways on the Hong Kong-based carrier's surprisingly profitable strategy of flying widebodies on Asian routes usually considered too short for such planes.



THIS PAGE, FROM TOP: PHOTOGRAPH BY JEFF MERMELSTEIN FOR BLOOMBERG BUSINESSWEEK; DANIEL J. GROSHONG/BLOOMBERG. OPPOSITE PAGE, FROM TOP: KIMIMASA MAYAMA/BLOOMBERG; JOCHEN ECKEL/BLOOMBERG; KEVIN PHILLIPS/GETTY IMAGES

flying in from Boston for shopping weekends. Once a jeweler visited the client with baubles worth a couple of million dollars and a gun for protection. On another trip, the banker booked a private session with designer Peggy Jennings, who has made clothes for Laura Bush and Hillary Clinton. She spent several hundred thousand dollars, give or take, over a year and a half, says von Sperling. "Back then, that was typical," she says, characterizing her situation at the time as "living like a rock star."

Today, von Sperling's shopping trips are far less splashy. In November, she hosted a family from Las Vegas. While her clients indulged, they focused on practical things. Two teenage daughters bought $400 Lanvin sneakers; the wife, a cashmere coat. "It was luxury shopping," von Sperling says. "But nobody was buying anything they didn't need. You don't need a sapphire necklace, but you might need a warm coat."

Many clients have embraced a do-it-yourself ethos, paying von Sperling's hourly fee for a consultation and then heading to New York's tony Bergdorf Goodman by themselves. They've also taken to shopping their closets, hiring her to find new looks for old clothes by dyeing a dress or cutting off sleeves instead of buying a new wardrobe.

As the U.S. economy recovers, consultants are betting job-seekers will want to update their appearance, as they have after previous slumps. "Even people who have good careers need to differentiate themselves," says Marks, a 25-year industry veteran. Already, she says, image consultants are targeting job fairs, both as paid gigs offering lessons on etiquette such as handshaking and as fertile ground for finding new clients.

Even as image consultants regroup in the U.S., interest in such services overseas is growing. Michelle Sterling, a former analyst for Banc of America Securities, says her New York-based Sterling Style Academy has attracted aspiring image consultants from more than 20 countries and that she added a class in Dubai last year. "This business does follow the economic trends," she says. "Women love to shop everywhere."
—*Matt Townsend and Ian Thomson*

The bottom line *Image consultants who help style affluent clients prospered during the boom. The fragile recovery has pinched their business model.*

Briefs

by Caroline Winter

Toshiba
Big 3D TVs, without the glasses



Toshiba plans to sell the world's first large 3D TVs that don't require viewers to wear special glasses. The electronics giant, which began offering glasses-free 12-inch and 20-inch 3D sets in Japan in December, will introduce screens that are 40 inches or larger sometime after April. Toshiba expects the new models to boost TV sales by 33 percent next fiscal year, with its North American market share rising about 2 points to 10 percent. Larger rivals Samsung and Sony sell 3D TVs, but viewers must use eyewear. Toshiba also plans to introduce TVs with Google software for Internet browsing.

Fiat
Mulling control of Chrysler

Italian carmaker Fiat, which owns 20 percent of Chrysler, may boost its stake to over 50 percent if the U.S. automaker opts for an initial public offering in 2011, says Sergio Marchionne, who helms both companies. Fiat acquired its stake as part of Chrysler's 2009 bankruptcy and has an option to buy an additional 16 percent after Chrysler repays U.S. and Canadian loans. Fiat could save as much as $2.7 billion if it exercises that right ahead of an IPO, according to UBS analysts. There are no plans to merge the companies, Marchionne says.

J.Crew
This deal isn't wrapped up yet

Urban Outfitters, Sears, and at least two private equity firms are considering bids for clothier J.Crew in a potential challenge to TPG Capital and Leonard Green & Partners' $3 billion buyout offer, according to people with knowledge of the matter. Rival offers may validate J.Crew's strategy of using a go-shop period to solicit competing offers after signing a preliminary agreement with the two firms in November, rather than conducting an auction. The New-York based clothing retailer, which is facing over a dozen lawsuits from shareholders over the terms of the November deal, must pay TPG and Leonard Green $27 million if it accepts a higher offer.

Thomas H. Lee Partners
More deals between buyout firms

Thomas H. Lee Partners is buying food marketer Acosta from private equity firm AEA Investors in a deal that values the company at more than $2 billion. Acosta, which helps companies promote and market their products, is at least the second such company in two months to switch private equity owners. Private equity firms are making deals with rivals after a two-year decline in leveraged buyouts left some firms with spare money to invest and others seeking to exit older deals. Secondary buyouts accounted for a record 24 percent of all leveraged buyouts by value last year, up from 8 percent in 2006, according to data compiled by Preqin.

Petrobras
Negotiating a path to Europe



Petrobras has confirmed it is in talks to buy Eni's $5.5 billion stake in Portugal's Galp Energia. Brazil's state-controlled oil company is offering $4.7 billion for the 33 percent holding, according to reports in the Portuguese press. Petrobras and Galp are partners in oil reserves off Brazil's coast, including the Lula field, which contains an estimated 6.5 billion barrels of recoverable oil and equivalents. The purchase would give Petrobras access to Galp's refineries in Portugal, allowing it to sell gasoline in Europe.

On the Move

LVMH Eric Marechalle named CEO of Kenzo • **Bank of Montreal** Chief Risk Officer Tom Flynn to become CFO in March • **Aveva Group** James Kidd appointed CFO • **BJ's Wholesale Club** Robert W. Eddy named CFO



The Chesapeake Bay spans over 200 miles, and its communities are home to millions of people. Every day, Siemens is helping improve the waters they depend on. That's why, after years of neglect, the bay is starting to come back. And it's just one example of the work Siemens is doing from coast to coast. Siemens purification and wastewater treatment technologies are helping municipalities big and small improve the health of their waterways. Somewhere in America, our team of more than 60,000 employees spends every day creating answers that will last for years to come.

siemens.com/answers

worldmags

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American Therapeutic mental health clinics

PHOTOGRAPHS BY CHRISTOPHER MORRIS FOR BLOOMBERG BUSINESSWEEK

Why Medicare Can't Catch the Fraudsters

▶ **One provider's claims were paid despite unusual billing patterns**

▶ **"It wasn't designed with these types of criminal attacks in mind"**

Six days a week, the elderly patients came in vans for mental-health group therapy sessions. They filed into outpatient clinics located mostly along South Florida's busy commercial corridors and in strip malls. The seven offices, operated by American Therapeutic, looked legitimate: Medical symbols adorned the windows and signs pronounced each "A Center of Excellence."

The operation, however, was a scam that bilked Medicare, the federal health program for the elderly and disabled, out of $83 million over eight years, according to a 13-count federal indictment in October of two companies and four individuals. Patients were plied with cigarettes and lunch, and some received $35 to sit in a clinic all day, prosecutors say.

Court papers name as the fraud's masterminds Lawrence S. Duran and Marianella Valera, the owners and managers of Miami-based American Therapeutic and another company, Medlink Professional Management Group, that handled the finances. They used the money to pay for a luxury condo on Biscayne Bay, jewelry, private school tuition, and a Maserati, the court documents say. Duran and Valera pleaded not guilty and their lawyers, Lawrence R. Metsch and Arthur Tifford, declined to comment.

Alleged scams like this are not new to the $500 billion Medicare program. What makes these accusations stand out is that officials at the Centers for Medicare & Medicaid Services (CMS), part of the Health and Human Services Dept., say they knew for years that something was amiss. The eight years it took to stop the alleged ring shows how difficult it will be for President Barack Obama to cut costs by reducing Medicare fraud, one goal of the health-care overhaul he signed in March 2010. "The system is broken," says Malcolm K. Sparrow, a professor at Harvard University's John F. Kennedy School of Government. "It wasn't designed with these types of criminal attacks in mind, and it can't cope with them."

Medicare until recently lacked the money to integrate data or do real-time analysis

In the three and a half years ending in June, Medicare paid $525 million to South Florida outpatient mental-health providers, almost 800 times the amount for New York and 78 times the amount paid in California. It didn't determine the reason for the imbalance because it was busy pursuing other fraud cases, says spokesman Peter Ashkenaz. Instead, Medicare kept paying the bills.

Outpatient mental-health care was supposed to save money by keeping Medicare patients out of hospitals. But the program is vulnerable to schemes that take advantage of re-

The company recruited patients from halfway houses, court papers say





gional claims processors that don't routinely compare notes–and miss upticks in billing. In this case, even after an antifraud contractor, SafeGuard Services, a unit of **Hewlett-Packard**, says it detected anomalies, officials didn't crack down.

A probe might have found what prosecutors later described in court documents: Some American Therapeutic patients being treated for mental health problems were so affected by dementia or Alzheimer's that they didn't know where they were. The company recruited patients by bribing managers at halfway houses and assisted-living facilities, according to court papers. From 2003 until October 2010, the clinics submitted almost $200 million worth of claims, of which about 42 percent were paid, according to the indictment.

There are no reliable figures for how much Medicare loses to fraud annually. Senator Tom Coburn (R-Okla.) estimates the loss from fraud, waste, and abuse at $60 billion, based on various studies. Peter Budetti, the agency's deputy administrator for program integrity, says only that there is "a lot" of Medicare fraud, and the more officials look, the more they find. Other Florida providers for years billed for intravenous drugs to treat HIV and AIDS patients, even though the services were not medically necessary or ever provided, a 2007 report by the HHS inspector general says.

The Government Accountability Office, the investigative arm of Congress, in 2009 reported that a spike in bills from several states for home health care was due in part to "fraudulent and abusive practices." The problem, says Senator Charles Grassley (R-Iowa), a frequent Medicare critic, is that the agency "is only geared to be a check-writing machine" and not a fraud fighter.

A Medicare strike force launched in 2007 by the Justice Dept. and HHS provides a sense of the scale of the problem: It has obtained indictments of more than 825 people who prosecutors say falsely billed Medicare for about $2 billion. The strike force repeatedly has been able to "detect fraud that Medicare has failed to notice," says Kirk Ogrosky, who until March 2010 was a federal prosecutor coordinating Medicare fraud cases and is now a partner at Arnold & Porter, a Washington law firm. "It is a phenomenon that is rarely seen in law enforcement–that the police call the victim to let them know that a crime occurred."

800%

How much South Florida's outpatient mental health tab topped New York's

That's what happened in South Florida with outpatient mental health, say law enforcement officials who faulted Medicare for failing to act sooner. The officials, who requested anonymity because they weren't authorized to speak publicly, say the Justice Dept. requested claims data and saw the suspicious pattern. The investigation began after a whistleblower filed a lawsuit that remains under court seal, the law enforcement officials say. Investigations of clinics beyond American Therapeutic have begun, and more prosecutions may follow, they say.

Cecilia Franco, head of the Medicare office in Miami, says her agency told Justice about the payment imbalance in South Florida years ago. The law enforcement officials say they aren't aware of any such reports. Laura Sweeney, a Justice Dept. spokeswoman, declined to comment. CMS spokesman Ashkenaz says the agency wants to avoid pointing fingers and would not say who at Justice was told, or when.

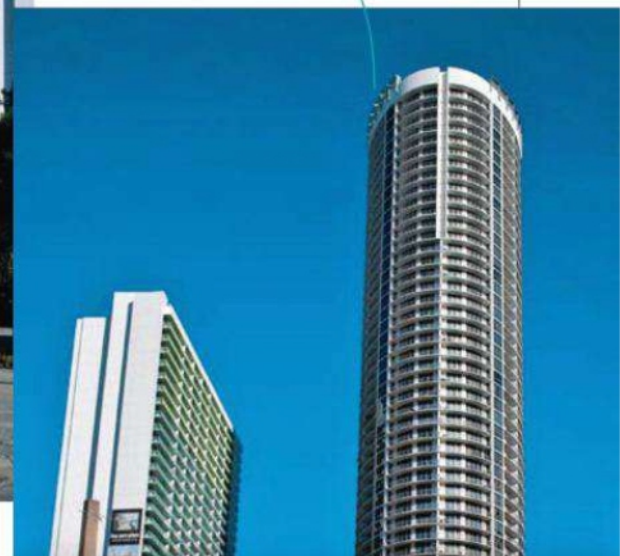
Detecting abnormal patterns is hard because Medicare's antifraud contractors serve specific regions and don't keep databases that allow for national comparisons. Medicare until recently lacked the money to create a nationwide database and do real-time analysis, says Kimberly Brandt, an attorney at Washington law firm Alston + Bird who directed a CMS fraud detection and prevention unit until June.

Medicare is now buying software to help it flag suspicious claims before they're paid, says spokesman Ashkenaz. Under the health-reform law, Medicare also has more power to screen providers, and in September proposed subjecting some to site checks and fingerprinting. The law makes it easier for Medicare to withhold payments when fraud is sus-

FROM TOP: PHOTOGRAPHS BY CHRISTOPHER MORRIS FOR BLOOMBERG BUSINESSWEEK; PRINCETON UNIVERSITY

Prosecutors say the proceeds paid for a condo on Biscayne Bay





pected, deputy administrator Budetti says. "While it is an easy thing to say what they should or could have done in the past," says Brandt, "the real key is what they are doing now that they have resources and authority" to address.

Those changes will help, says Joseph Antos, a health policy analyst at the American Enterprise Institute for Public Policy Research, but they won't "get at the fundamental problems" of paying claims first and asking questions later, when the money is long gone.
—Justin Blum

The bottom line *Attempts to curb Medicare fraud are hampered by the inability of claims processors and other contractors to compare notes.*

Online Advertising

The Geek Who's Policing Your Privacy

▶ Princeton's Ed Felten advises the FTC on regulating Web marketers

▶ "A one-person truth squad who understands the technobabble"

Internet giants such as **Facebook** and **Google** hope to make serious money over the next decade by allowing their advertisers to target pitches to consumers based on online behavior. Potentially standing in the way is Edward W. Felten, who was just named to be the Federal Trade Commission's first chief technologist.

The 49-year-old Princeton University computer science professor has been hired by FTC Chairman Jon Leibowitz to help find the middle ground between consumer groups' demands for digital privacy protections and marketers' hunger for unfettered access to consumers. "He is a rocket scientist who can explain technical issues to the non-cognoscenti and serve as an ombudsperson across the agency," Leibowitz says.

At stake is an online advertising market that's projected to grow to $40 billion by 2015, from about $26 billion in 2010, according to Brian Wieser, director for global forecasting at MagnaGlobal, a unit of Interpublic Group, a New York-based owner of advertising agencies.



"As an engineer, I can have a different kind of conversation with people"

Felten has been meeting with industry experts and researchers since his November appointment. His technology background helps bridge the language gap between the public and industry, Felten says. "As an engineer, I can have a different kind of conversation with people," he said during an interview at the commission's headquarters. Felten is taking a one-year leave of absence from Princeton and his position as head of the university's Center for Information Technology Policy. He will be spending less time writing his blog, Freedom to Tinker.

Felten's first task is to help the FTC convince Internet companies to voluntarily let consumers opt-out from having their browsing data collected by Web marketers, a move the FTC called for on Dec. 1. The question of how best to accomplish this "is something we are still discussing," Felten says. He is studying blocking mechanisms, including a tracking protection option offered in **Microsoft**'s Explorer 9 browser, released on Dec. 7, and Google's advertising preferences manager. Researchers at Stanford University also have developed a way for browsers to notify websites that a visitor doesn't want personal information collected. "These are feasible options," Felten says.

The better approach, Felten says, may be to give the consum-

er—not companies—the choice of how much information can be collected. Data that people volunteer "may be more accurate than what the company has deduced about the user," Felten says. "And the user may have a higher comfort level deciding what information to provide rather than worrying about what inferences might be made from what they've gathered."

Known for cracking the music industry's digital-copyright protection code in 2000 (in response to a challenge from the music industry), Felten boasts a résumé that includes exposing security weaknesses in electronic voting machines. In 1998 he testified for the government in its antitrust case against Microsoft, saying that the company's Internet Explorer Web browser could be separated from the Windows 98 operating system without impairing the functionality of Windows.

"For years online marketers have tried to pull the wool over the eyes of the FTC," says Jeff Chester, executive director of the Washington-based Center for Digital Democracy, a consumer advocacy group. "Now the FTC has a one-person truth squad who understands the technobabble."

Behavioral advertising, which targets individual consumers based on their interests, is "the Holy Grail for marketers," says Lisa Sotto, a privacy lawyer with Hunton & Williams in New York who advises companies on advertising, data, and security matters. "Everybody is trying to figure out what the future looks like, both in terms of technology and the legal guidelines," Sotto says. "Companies should include him in their discussions, and not view him as an adversary."

$40
BILLION

The estimated size of the online advertising market by 2015

Consumer advocates hail Felten's appointment as a sign the government is getting serious about regulating online advertising. So far the online industry has also welcomed Felten to the job. "We respect his work and think he was an excellent hire for the FTC," says Google's privacy spokeswoman, Christine Chen. The good feeling could dissipate, however, as companies face mounting calls from regulators, consumer groups, and lawmakers to further safeguard privacy on the Web.
—Sara Forden

The bottom line *By hiring Princeton's Felten, the FTC shows it's serious about regulating targeted ads, the Holy Grail for Web companies.*

Death and Taxes



It's the ultimate revenge. Milliken & Co. Chairman Roger Milliken died on Dec. 30 at age 95, hours before the estate tax jumped to 35 percent on Jan. 1. In 2003, *Forbes* estimated his fortune, derived from the Spartanburg, S.C., maker of textiles and chemicals, at $1 billion. Now it passes tax-free to his heirs. "His timing was impeccable," says Jock Nash, his trade lobbyist. In 1916, his grandfather, company co-founder Seth Milliken, gave company shares to his children before dying, hoping to avoid a newly created estate tax. The Supreme Court later ruled those gifts were subject to the tax. Roger Milliken, a staunch Republican, opposed unions and trade deals, especially NAFTA. "He lived out every minute of every day of his life," says company spokesman Richard Dillard.
—Ryan J. Donmoyer

Regulation

Nasdaq's Secret Agent Derivatives Campaign

▶ **The exchange wants to limit banks' ownership of clearinghouses**

▶ **"Those banks can decide to take their business elsewhere"**

As Congress was considering forcing most derivatives transactions to go through a clearinghouse for the first time, **Nasdaq OMX**, the New York-based stock exchange, saw a huge opportunity. It set its sights on winning a larger share of the lucrative business of clearing interest rate swaps. Such swaps are used to hedge against higher borrowing costs or to speculate on interest rate moves and represent a $348 trillion market, according to the Bank for International Settlements.

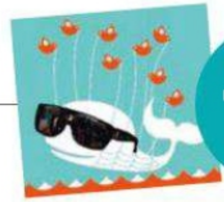
Just one problem: Clearinghouses, which process trades and guarantee payment in case either party defaults, are dominated by large Wall Street banks that are also among Nasdaq's biggest customers. To get around that uncomfortable fact, Nasdaq officials devised a stealth lobbying campaign to persuade Congress and regulators to limit bank ownership of clearinghouses.

"It is dangerous to state openly what they feel," says Michael Greenberger, a former Commodity Futures Trading Commission official who is now a University of Maryland law professor, "because those banks can decide to take their business elsewhere." The resulting skirmish is a vivid illustration of how companies sometimes turn to Washington to gain an advantage via regulation that they can't get in the marketplace, says Greenberger.

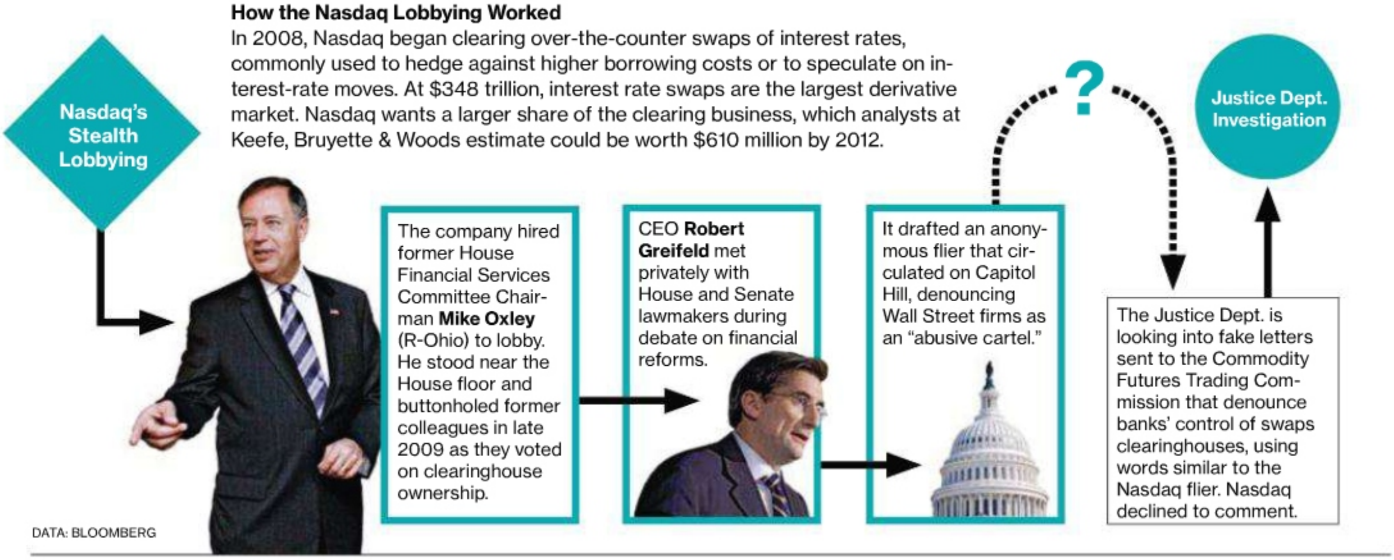
The dominant player in interest rate clearing is London-based **LCH.Clearnet Group**, which is majority-owned by the world's largest banks, including **JPMorgan Chase** and **Goldman Sachs**. The banks oppose strict ownership limits, arguing that clearinghouses need owners with enough capital and expertise to weather market disruptions. "The most likely sources of both are swap dealers," the Securities Industry and Financial Markets Assn., a trade group led by big banks, wrote in a November letter to regulators. Chicago-based **CME Group**, the world's largest

AP PHOTO; OPPOSITE PAGE: BLOOMBERG (3); AFP/GETTY IMAGES

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The ad network for Twitterati page 32 ▶



futures exchange, also clears interest rate swaps but is much smaller than LCH.Clearnet. Nasdaq's two-year-old clearinghouse for interest rate swaps, the **International Derivatives Clearing Group**, is even smaller, according to the exchanges.

Nasdaq, consumer advocates, and unions say the banks' dominance of both trading and clearing derivatives has driven up costs for companies that need to hedge the risk of changes in commodity prices or interest rates. The Justice Dept., in Dec. 28 letters to regulators calling for stringent limits on clearinghouses and derivatives trading platforms, also raised anticompetitive concerns.

As part of the exchange's lobbying campaign, Nasdaq CEO Robert Greifeld came to Washington during the financial regulatory overhaul debate and met personally with lawmakers, according to two congressional aides who were present and requested anonymity because the meetings were private. Michael Oxley, a former Ohio representative who advises Nasdaq's board, stood near the House floor during a vote on an amendment limiting bank ownership; reporters saw him buttonholing fellow Republicans.

An anonymous flier, titled "Myths That the TARP Banks Are Spreading About the Lynch Amendment," circulated on Capitol Hill about a measure by Representative Stephen Lynch (D-Mass.) to limit bank ownership of a clearinghouse to 20 percent. The flier, which Nasdaq eventually acknowledged drafting, denounced Wall Street firms as an "abusive cartel."

The final version of the Dodd-Frank law lets regulators decide where to set ownership limits. Nasdaq representatives have visited the CFTC and the Securities and Exchange Commission to discuss the issue, according to the agencies' websites. When the CFTC in October proposed two options for ownership limits, Nasdaq didn't submit a written response. The agency, however, did receive letters supporting Nasdaq's position that were purportedly from Arkansas residents, including a rural county sheriff and a Burger King franchise owner.

Bloomberg News reported in November that those letters were forgeries generated as part of a campaign by the **Dewey Square Group**, a Boston-based public affairs firm. The Justice Dept. is investigating. The fake letters, which a Dewey Square principal, Ginny Terzano, says were unauthorized and sent by a subcontractor without the firm's knowledge, contained the same message that Nasdaq has been pushing in Washington as it tries to muscle its way into the derivatives business. Nasdaq's chief spokesman, Frank De Maria, declined to say whether the exchange hired the firm responsible for the letters. *—Clea Benson, Robert Schmidt, and Silla Brush*

The bottom line *To bulk up its swap clearing business, Nasdaq tried to use Washington to get what it couldn't win in the marketplace.*

Higher Education

The States Take Aim At Tenured Professors

▶ Retirement incentives are being offered to cut costs

▶ "These buyouts will become more common"

At 66, Darrell Fasching wasn't planning to retire from his job as a professor of religious studies at the University of South Florida in Tampa. He changed his mind when he was offered a year's salary—about $90,000—to step down and give up tenure rights earned over almost three decades at the school. By taking the cash, he joined hundreds of professors at public universities across the U.S. who have been coaxed into retirement with offers of as much as two years' pay.

Faced with 2012 deficits estimated at a total of $140 billion, according to the Center on Budget and Policy Priorities, states are looking to their university systems for savings, even if it means circumventing the once-sacrosanct tenure system. "Most states have horrific budget problems, and they haven't dealt with the kinds of cuts in higher education that are going to be necessary," says Roger Meiners, who teaches economics at the University of Texas at Arlington and has written

a book about tenure. "These buyouts will become more common."

The push to replace expensive tenured professors comes after states cut support for colleges and universities. Funding fell 3.5 percent in fiscal 2010, to $75.2 billion, after a similar drop in 2009, according to the Center for the Study of Education Policy at Illinois State University in Normal. The buyouts also make business sense: Pay for tenured professors averages $117,000 a year at the top 200 U.S. public universities, according to the American Association of University Professors. Annual contracts for replacement instructors cost an average $52,500, the group said in an April report.

Florida, which may face a deficit of $3 billion-plus in the next fiscal year, cut funding for its 11 public universities by 22 percent from 2008 to 2010. Fasching says the state's bleak fiscal outlook led him to grab the buyout. "Things aren't looking any better for next year," he says.

Texas A&M University in College Station persuaded 104 professors to retire, says Karan L. Watson, the interim provost. At the University of Texas in Austin, 27 of 88 eligible professors–those whose age and years worked added up to 93 or more–in the College of Liberal Arts accepted buyouts totaling two years of salary, says Gary Susswein, a spokesman. The buyouts may save the two Texas schools more than $15 million a year combined, say Watson and Susswein.

Even some private colleges and universities, which have cut budgets because of falling endowment returns and rising competition for tuition dollars, are considering culling senior faculty. At Harvard, retirement incentives were offered to 176 professors 65 or older with at least 10 years on the job, according to last year's annual faculty report. It said 46 of them, with a median age of 70, accepted.

John Curtis, research director at the American Association of University Professors, warns that the departure of the most seasoned professors may prove damaging down the line. "Experienced and active faculty members who will be leaving and replaced in the short-term are going to be followed by people who are much more transient," he says. Ⓑ
—David Mildenberg and Janet Lorin

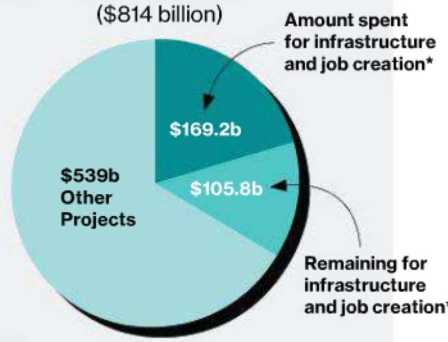
***The bottom line** State universities and even some private colleges are culling senior faculty members to trim budgets.*

Stimulus

The Myth of the "Shovel-Ready" Project

Some of the largest U.S. cities still haven't spent half or more of the federal stimulus funds designated almost two years ago for job creation. While some spending was purposely deferred, audits also point to delays resulting from bureaucratic snafus, the complexity of the work, and shortages of federal and local staffers to get the money out. The slow payouts may be inhibiting the recovery, some critics say. "People who are unemployed want jobs today, not next year," says Los Angeles Controller Wendy Greuel, who is running for mayor in 2013. —*Christopher Palmeri*

Total stimulus
($814 billion)



*Includes local governments, nonprofits, and businesses

Philadelphia

ALLOCATED **$251 million**
SPENT (THROUGH 9/30) **$40 million**
16% USED

Philadelphia was awarded 46 percent of its stimulus money in 2010. "Innovative projects take time to advance, and the city has been careful to avoid fraud," says Mark McDonald, a spokesman for Mayor Michael Nutter. Projects under way include the first solar panels on a municipal facility, a water-treatment plant.

Los Angeles

ALLOCATED **$630 million**
SPENT (THROUGH 10/31) **$181 million**
29% USED

Audits by Controller Wendy Greuel found bureaucratic mixups and employee cutbacks led to spending delays for such projects as street resurfacing and installation of left-turn signals at intersections.

New York City

ALLOCATED **$7.2 billion***
SPENT (THROUGH 9/30) **$3.9 billion**
54% USED

Most of the remaining money will be spent to retain teachers whose jobs might be lost to budget cuts, and on low-income health programs, says mayoral spokesman Marc LaVorgna. Construction projects, such as remodeling of a Staten Island ferry terminal, continue.

*Includes $3.7 billion for Medicaid and other social services

Chicago

ALLOCATED **$2.2 billion***
SPENT (THROUGH 9/30) **$1.3 billion**
59% USED

The city is still working on projects that include road resurfacing, installation of security cameras at Midway Airport, and renovation of an elevated train station, all of which the city claims saved or created 3,511 jobs in the third quarter of 2010 alone.

*Includes $1 billion for schools

DATA: U.S. RECOVERY ACCOUNTABILITY AND TRANSPARENCY BOARD, RECOVERY.GOV, CONGRESSIONAL BUDGET OFFICE

Until Neil Armstrong walked on the Moon, he would not rest. Nor would his crew. (Sea of Tranquility, 1969.)



Until you get to where you want to be.

You only need to know one thing.

It isn't that our global reach is extensive.

Although that's comforting to hear.

It isn't that we win awards for our services.

Although we do. Often.

It isn't that we have access to resources, giving us strength and depth across equities, fixed income, structured products and currencies.

Although that, too, is nice to know.

It isn't that.

In fact, it's none of the above.

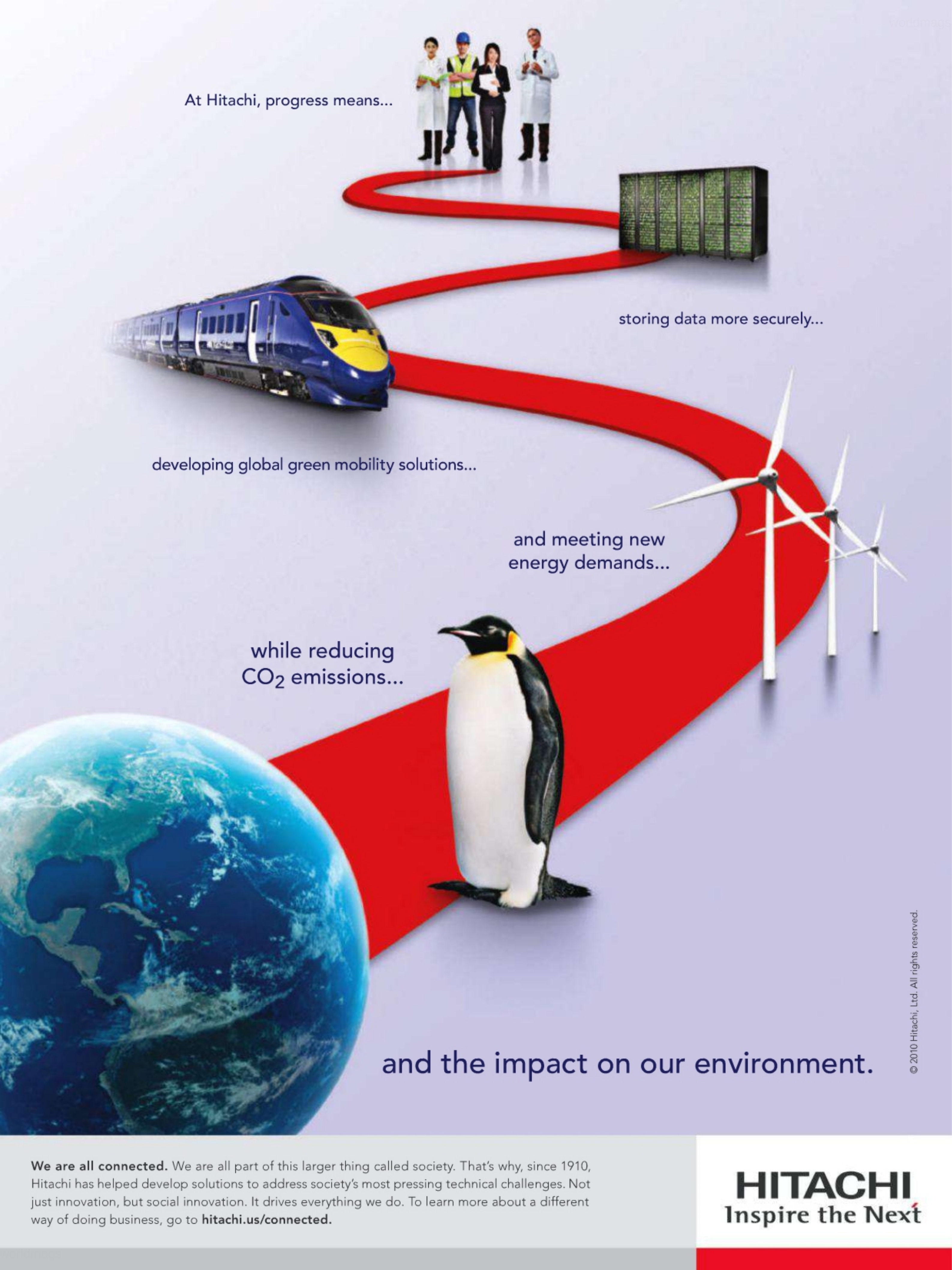
It's one simple thing.

Until you achieve your goal...

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HITACHI
Inspire the Next

Contents ▶ An ad network that pays celebrities $10,000 per tweet 32 ▶ Google's search for a mobile payments network 33 ▶ Dolby woos the earbud generation 35 ▶ Chipmaker Atheros has a $3.1 billion payday 36 ▶ Innovator: George Huber's biomass breakthrough 37 ● Edited by Barrett Sheridan

Technology



The Great Tablet Grab of 2011

▶ **The Consumer Electronics Show signals the tablet is the new PC**

▶ **"Apple does not have a corner on the market for innovation"**

For the last few years, the International Consumer Electronics Show, held each January in Las Vegas, has been a disappointment. In 2009 tech's most important annual gathering found itself in the icy grip of a global recession, with attendance down by 30,000. Last year the highlights included a new class of 3D televisions that are now on sale for deep discounts. Did you buy one? Apparently no one else did either.

That's the setup for this year's show, on Jan. 6-9, which is shaping up to be one of the most significant in recent memory. Many of the prevailing trends in high tech—often tidily summarized by the word "convergence"—are now mature enough to start changing the way regular people interact with technology. The HDTVs and in-car entertainment systems on display at CES will connect to the Internet; movies, music and games will make their way to all manner of devices as the PC finally relinquishes its spot as the dominant way to access multimedia and the Web. Embodying these trends, and sure to draw most of the attention at the conference, is a torrent of new tablets from **Asus**, **HTC**, **LG Electronics**, **Motorola**, **Toshiba**, and many others—each hoping to replicate the success of **Apple**'s eight-month-old iPad.

The stakes of the emerging tablet wars are huge. Apple has an early lead, with an estimated 10 million iPads sold in 2010, and is likely to keep it. But analysts believe the market is set to explode. The research firm iSuppli predicts 57 million tablets will be sold in 2011 and 171 million in 2014. "These companies aren't trying to steal away from Apple. They are betting the overall pie will expand," says Richard Doherty, research director at the Envisioneering Group, who estimates that more than 100 tablets are being introduced at CES this year.

As with smartphones, **Google** and its hardware partners, including South Korea's LG and Motorola, are in the best position to loosen Apple's grip. At CES, Google was expected to demonstrate a forthcoming version of its mobile Android operating system, called Honeycomb, customized for tablets. Microsoft, too, was expected to preview a version of its operating system that will run across all types of devices, from phones to PCs and tablets, and is compatible with low-power, mobile-device chips called ARM processors. "Two of the most influential companies in the world are going to put a stake in the ground and say this is your personal computing platform going forward," says Jen-Hsun Huang, chief executive officer of graphics and mobile chipmaker **Nvidia**.

For Microsoft, this year's CES is ➔

ILLUSTRATION BY JENNIFER DANIEL

both an opportunity to make up for lost time and a reminder of a painful past. At CES in previous years the company has demonstrated duds such as Internet-connected watches and $12,000 multitouch tables. Last year, CEO Steve Ballmer showcased a tablet running Windows, made by **Hewlett-Packard**. It went on sale in late 2010 and appealed only to a few business buyers. Windows "is still kind of heavy and optimized for devices with a physical keyboard," says Yongseok Jang, vice-president for business strategy at LG Electronics. His company plans to show an Android-powered tablet at the conference.

The new tablets will come in a variety of shapes and sizes. Some will have only Wi-Fi access, and others will also connect to speedy new 4G networks. While the iPad has no camera, many of the new tablets have two—one in the front, one in the back. Toshiba, the Japanese electronics giant, plans to announce an as yet unnamed tablet with a 10-inch screen, two cameras, and a removable battery. **Vizio**, the Irvine (Calif.) company that has seized a lead in the U.S. market for HDTVs, is unveiling an 8-in. tablet with a high-resolution screen and a front-facing camera for video conferencing.

Both Toshiba's and Vizio's tablets will run Android, but neither company wants to be confined to selling undistinguished, me-too hardware. They also want a piece of the highly competitive market for mobile software apps. Toshiba says it will introduce its own e-book store and marketplace for tablet applications, while Vizio has created an interface to allow users to watch the same content and play the same games across multiple Vizio devices. Both companies will have a challenge getting customers to use their offerings rather than more popular and familiar ones in the apps marketplace provided by Google.

Chinese manufacturer **Lenovo** has a unique approach with what it calls its IdeaPad U1 Hybrid with LePad slate. It's actually two computers in one—a slick, 10.1-in. Android tablet that becomes a PC running Windows 7 when it connects to a keyboard. "We're showing that Apple does not have a corner on the market for innovation," says Peter Gaucher, Lenovo's executive director for mobile Internet devices.

Many past technology battles highlighted at CES have been bad for consumers—such as the Blu-ray vs. HDTV format wars, which left some early adopters stranded with useless devices. Competition in tablets should drive down prices, limit Apple's near-monopoly on digital content distribution, and stimulate a round of creativity among the small developers who write applications for mobile devices. At the last two CESes, what happened in Vegas pretty much stayed in Vegas. Not this year.

—*Brad Stone with Cliff Edwards*

The bottom line *Roughly 100 tablets are being introduced at this year's CES. They're becoming a viable alternative to PCs.*

Social Media

And Now, a Tweet From Our Sponsor

▶ **Ad.ly signs up celebs like Snoop Dogg to pitch products on Twitter**

▶ **"The most effective ones can get six figures a year"**

In the 1980s she was Punky Brewster, the star of an **NBC** comedy about an orphan. Today, Soleil Moon Frye is a 34-year-old mother of two and a power marketer for **Ad.ly**, an advertising agency that pays actors, athletes, and musicians to promote products through micromessaging service **Twitter**. Two days before Christmas, Moon Frye's 1.4 million followers learned that THQ's uDraw tablet, which lets kids draw using a Wii video game console, is "a must for any family night!"

Celebrities have been endorsing products since before talkies. Ad.ly, a 22-person operation run out of a small suite of offices in Los Angeles, is pioneering what it calls the "micro-endorsement." Since its launch in September 2009, it has crafted more than 20,000 endorsements for more than 150 brands, including **Sony**, **Best Buy**, and **Old Navy**. The plugs, which adhere to the service's 140-character limit, are delivered through the Twitter streams of the Kardashian sisters, rapper Snoop Dogg, and more than 5,000 other personalities ranging from A-list to D-list.

The ad campaigns are a little on the micro side themselves. On a recent day in late December, Ad.ly staffers were at work putting together proposals for a $100,000 package for a handheld, digital projector from **3M** and a $50,000 campaign for **CBS** talk show *Dr. Phil*. For each campaign, Ad.ly tries to match the product with the best fit from its stable of celebrities, though advertisers have the final say as to who promotes their products. Pitches contain small labels indicating they're

ILLUSTRATION BY OLIVER MUNDAY; GETTY IMAGES (5); AP PHOTO (1)

Twitter, Twitter, Little Stars

Ad.ly crunched the numbers and provided *Bloomberg Businessweek* with the names of its most effective celebrity promoters on Twitter, as measured by clicks on their sponsored tweets. Below, a partial list:






Lauren Conrad	Kim Kardashian	Khloe Kardashian	Michael Ian Black
Followers: 1,445,149	**Followers:** 5,684,204	**Followers:** 2,174,265	**Followers:** 1,580,065
Sponsors: Sony Pictures, *Glee*, LivingSocial	**Sponsors:** Rebecca BonBon, Charlotte Russe, Nestlé	**Sponsors:** Old Navy, Best Buy, Bing (Microsoft)	**Sponsors:** Sony Pictures, Norton AntiVirus, Arby's
Sample tweet: "I wonder if the celebs will dress the part! Check out @BurlesqueMovie the red carpet premier"	**Sample tweet:** "Cute @iloveRBB Paparazzi shot of ur new line! Luv it, Rebecca Bonbon, U adorable puppy!"	**Sample tweet:** "Want to know how Old Navy makes your butt look scary good? Ask a Kardashian ;)"	**Sample tweet:** "They say boys will be boys, some longer than others. This weekend, see *Grown Ups*, now playing! Get tix here"

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ads, as required by the Federal Trade Commission.

"Celebrities can be great influencers, whether they're on TV or tweeting," says Arnie Gullov-Singh, 38, Ad.ly's chief executive officer. A pair of twentysomething staffers craft most of the promotional tweets in the voice of the celebrity pitchmen. In hawking the **Toyota** Sienna, rapper Snoop Dogg tweeted that "these homies know the deal" and wondered if oversized rims would fit on the minivan's wheels. Businessman Mark Cuban, another celebrity on the roster, tweeted that it "looks like I need to invest in a fleet of Sienna minivans."

The celebs earn a flat fee per tweet that ranges "from $1,000 to mid-five figures," says Gullov-Singh. With more than 5.6 million followers, reality TV superstar Kim Kardashian collects "in the ball park" of $10,000 per tweet, he adds, "but her price keeps going up. The most effective ones can get six figures a year, and in some cases six figures a quarter."

For Cuban, who's already a billionaire, joining Ad.ly's network wasn't a way to make cash but rather "something that I wanted to learn more about," says the Internet entrepreneur. Allowing Ad.ly to ghostwrite his tweets "was painful at first, but easier and easier because the products and services are respectable."

Cuban says letting Ad.ly tweet for him "was painful at first"



Jenny McCarthy

Followers: 229,336

Sponsors: Toyota Sienna, Groupon, Arby's, LivingSocial

Sample tweet: "Hey ladies, who might be PMSing like I am, or just hungry dudes, I heard @Arbys you get a free JR Deluxe TODAY!!!"



Mark Cuban

Followers: 283,359

Sponsors: GE Ecomagination, AT&T, *Man v. Food*

Sample tweet: "Up and coming filmmakers challenged themselves to lend a creative perspective to Ecomagination. Amazing videos!"

Celebrities can veto tweets for products they don't want to promote or tinker with the language from Ad.ly's copywriters. Says Lauren Conrad, former star of MTV reality show *The Hills* and another celebrity in Ad.ly's roster: "I am very selective about what I endorse."

Twitter is testing its own advertising service, which could compete with Ad.ly for the attention of sponsors. A more direct competitor is four-year-old **Izea**. The Orlando company began by promoting brands on blogs and last year expanded to Twitter. It now has a network of more than 100,000 tweeters who promote products for anywhere from 10¢ to more than $2,500 per tweet, according to CEO Ted Murphy. Some celebrities or their managers negotiate directly with the sponsors and avoid using intermediaries such as Ad.ly.

Ad.ly is backed by $6 million in venture capital and was founded by 24-year-old Sean Rad, a serial entrepreneur. The company is diversifying into other social media sites. It recently began offering what it calls a celebrity bundle, in which brand promotions appear not just in celebrities' Twitter streams but also on their fan pages and in display ads on **Facebook**.

"I can see great upside and great risks for a brand putting their message on Twitter," says Debbie DeGabrielle, chief marketing officer of Visible Technologies, which assesses social network traffic for clients such as FedEx. "If the celebrity is aligned with your brand, that's great," she says. "But if you're Toyota, will Snoop Dogg talking about 22-inch wheels drive away your women buyers?" Toyota spokeswoman Zoe Zeigler says the company "did not have any issues with the copy."

Dave Rosner, a senior vice-president at ad agency **Initiative**, has used Ad.ly to promote his clients' products, including a film from **Lionsgate Entertainment** and a car from **Kia**. "They give us a streamlined way of signing celebrities, where an agreement can sometimes take a long time," he says. Rosner is not yet totally convinced the campaigns are effective, but he thinks the experiment is promising. "We're still here," he says. —*Ronald Grover*

***The bottom line** Ad.ly operates a network of more than 5,000 celebrities willing to shill for brands through their Twitter accounts.*

Mobile Payments

Google's Search For a Digital Wallet



▶ **The search giant is working on a payments service for smartphones**

▶ **Near-field communication, or NFC, "could displace the cash register"**

Since mid-December, **Google** has been handing out hundreds of kits to local businesses in Portland, Ore., as part of a trial called Hotpot. The kits include window decals that use near-field communication, a low-power technology that beams and receives wireless information from up to four inches away. When customers with NFC-equipped phones—including the latest models running Google's Android software—scan one of the window decals, they'll see the business's operating hours, reviews, and other relevant information. "It's something that helps local businesses," says Sara Heise of Voodoo Doughnut, one of the merchants taking part in Hotpot. "It'll allow us to interact with our customers more, especially the younger, texting generation."

It's also the latest sign that 2011 will be the year of NFC. Google is considering building an NFC-based wireless payment service in the U.S. that could make its debut this year, say two people familiar with the plans. The technology would let customers pay for items by passing a smartphone over a small reader. A single NFC chip would be able to hold a consumer's bank account information, gift cards, loyalty cards, and coupons, say the two people, who requested anonymity because the plans aren't public. Google's NFC scheme includes an advertising component that would allow merchants to beam a coupon or other reward to customers while they are shopping.

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Technology

Smartphone owners can already complete transactions on the go by downloading applications. PayPal's iPhone app, for instance, lets users send money to other accounts. NFC technology can streamline such transactions. Phones with NFC don't require users to launch an application; they simply wave or tap their phone against a reader and enter a PIN number on it to authenticate the purchase.

Any NFC offering from Google will face tough competition from the start. In November, **Verizon**, **AT&T**, and **T-Mobile** formed a venture called ISIS that plans to launch an NFC-based payments service by 2012. **Visa** is testing several mobile payment technologies, including NFC, and plans a commercial roll-out late this year, according to Bill Gajda, Visa's head of mobile innovation. PayPal, a division of **eBay**, may test an NFC service in the second half of 2011.

Other Silicon Valley companies may be working on the technology, too. **Apple** has filed a patent for a process to transmit money between cell phones using NFC. The iPhone maker also recently lured NFC expert Benjamin Vigier away from **mFoundry**, a startup that helps banks build mobile payments applications. "It's a land grab," says Jaymee Johnson, a spokesman for ISIS. "Folks are sort of jockeying for position." The prize for whoever wins the race is a dominant position in a small but fast-growing market that "could displace the cash register," says Charles Walton, chief operating officer for NFC chipmaker **Inside Secure**. IE Market Research estimates that, by 2014, NFC-based payment systems will account for a third of the $1.13 trillion in worldwide mobile transactions.

Quoted

"We are moving forward and trying to be productive individuals."
—Cameron Winklevoss, who recently decided, along with his twin brother, Tyler, and partner, Divya Navendra, to continue their legal fight against Facebook. They claim Mark Zuckerberg stole the idea for a social network from them.



Google wouldn't comment on its plans for an NFC payments service. At a conference in November, Google Chief Executive Officer Eric Schmidt enthused about NFC, saying it will "eventually replace credit cards." In mid-December, Google bought Zetawire, a Canadian startup with several NFC patents, including a method for diners to split and pay a restaurant bill using their mobile devices.

In launching a payments service, Google would have the advantage of its swiftly growing base of Android mobile phone users. Every day, some 300,000 people activate Android phones, and they accounted for more than 25 percent of the new smartphones shipped

JULIEN M. HEKIMIAN/GETTY IMAGES



in the third quarter of 2010, according to researcher Gartner. The latest version of the company's Android mobile operating system, dubbed Gingerbread, is the first one capable of reading NFC tags. Updates to the software later this year will let Android phones transmit information using NFC as well, says Andy Rubin, Google's vice-president of engineering.

For an NFC payments service to work, Google needs to convince not just smartphone users but also merchants, who have to install NFC readers to process mobile payments. Hotpot, which Google has been promoting at Portland Trail Blazers basketball games and around the city, introduces them to the technology. "We are going to start expanding into more and more cities in the near future," says Lior Ron, group product manager for Hotpot. "We want to make it national." —*Olga Kharif*

The bottom line *Google is considering joining the crowded mobile payments field. NFC technology could turn its Android phones into checkbooks.*

Digital Audio

Surround Sound for The Earbud Generation



Dolby started making software for PCs in 2005

▶ **Dolby's PC software improves audio quality, but kids might not care**

▶ **People don't sit around a "shag rug room, smoking a joint, listening"**

Bob Walters, head of the 300-member Bay Area Audiophile Society, has spent around $50,000 buying stereo equipment for the dedicated listening room in his home. But Walters, 53, can't persuade his nine-year-old daughter to ditch her more modern setup. "She doesn't want to listen to the song on my system," he says. "She wants to watch the **YouTube** video."

Walters' daughter is representative of a generation content to listen to low-fidelity digital tracks on cheap earbuds. That's a challenge for **Dolby Laboratories**, the San Francisco company famous for its theatrical surround sound, which made its debut in Francis Ford Coppola's *Apocalypse Now* in 1979. Dolby's latest release–a software program that converts low-quality PC audio to surround sound–is an effort to bring its technology to a new audience and train those listeners to appreciate high-quality sound.

The fourth iteration of Dolby's software for PCs, released on Jan. 4, is included in operating systems such as **Microsoft**'s Windows 7. No matter how tinny the laptop speakers or low-quality the audio, the software turns stereo recordings into 5.1- or 7.1-channel

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Divya Gugnani owns the culinary web company Behind the Burner; and for her, Booming is getting paid faster. After using social media to reach 140,000 subscribers in just two years, Divya needed her cash to flow as rapidly as her company was growing. So she started invoicing with AcceptPay,® a new online payment solution from American Express OPEN. Now her advertisers have more ways to pay, and she's getting paid around three weeks faster. Get your business Booming at open.com.

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Still putting out fires at Bank of America page 39 ▶



sound—meaning the audio seems to come from different places, creating virtual surround sound. It also promises to make movie dialogue clearer, keep volume levels consistent, and minimize distortions caused by weak speakers.

Dolby is confronting a market that each year has fewer and fewer audiophiles like Walters. "I don't see people sitting around somebody's shag rug room, smoking a joint, listening," says Faith Popcorn, chief executive officer of marketing consultancy Faith Popcorn's BrainReserve. **Sony**'s Walkman, introduced more than 30 years ago, trained consumers to prioritize convenience over sound quality. **Apple**'s iPod and other MP3 players have accelerated the trend, Popcorn says.

The numbers bear her out. The Consumer Electronics Assn. (which runs the Consumer Electronics Show held this month) estimates that more than a third of the $2.91 billion spent on home audio equipment last year went to docking stations for iPods, iPhones, and other devices that play highly compressed files with sound quality that isn't as good as compact disks or records. Sales of so-called home theaters in a box, or surround sound systems that include five speakers, a subwoofer, and a receiver, declined 9 percent, according to the CEA. Dolby is "trying to position themselves for online media, whether it's streaming music or movies," says Kerry Rice, an analyst with Wedbush Securities. "But I don't know if that propels demand—'Oh my gosh, I've got to go out and get this new PC that has this 7.1 surround sound.' "

It may not matter: Dolby doesn't sell directly to consumers. It licenses its software for use in Windows and other operating systems. Dolby's push into PCs so far has been successful. The PC software, first announced in 2005, now accounts for 36 percent of total licensing revenue. The division's sales were up 19 percent, to $710.5 million, last year, helping send the stock up 40 percent.

Mary Anderson, the director of marketing for Dolby's PC business, agrees that people's behavior has changed. She adds: "Just because your behavior changes doesn't mean you don't expect the same quality." —*Ryan Flinn*

The bottom line *Although Dolby's new PC software brings virtual surround sound to laptops, many consumers put convenience over quality.*

Semiconductors

Silicon Valley's Other Craig (Barratt) Cashes In

▶ **Wireless chipmaker Atheros is sold to Qualcomm for $3.1 billion**

▶ **"The irony is that Intel made Atheros in a way"**

If conventional wisdom had its way, **Atheros Communications** would have ended up as yet another mound of chip startup roadkill. Not only did it seek to do something new, risky, and expensive with its wireless chip offerings, but it brushed up against **Intel** and its near-bottomless coffers. Far from going on life support, Atheros survived—and did well enough to tempt **Qualcomm** into acquiring it for $3.1 billion in cash.

After a day of rumors, Qualcomm confirmed the purchase on Jan. 5. It paid $45 per share, a 29 percent premium over Atheros's average trading price during the last month. The deal is Qualcomm's biggest ever and gives the mobile technology giant a direct path to expansion in a number of growing markets, including Wi-Fi, Bluetooth, GPS, and systems that let Internet data flow through home electrical networks, known as powerline networking.

In announcing the acquisition, Qualcomm's chief executive officer, Paul E. Jacobs, noted that Atheros delivers a sales force and wealth of products aimed at consumer electronics and home networking. He says such technology will complement Qualcomm's Snapdragon chip, which sits inside many of the flashiest smartphones based on **Google**'s Android software, and create demand for new devices based on the chip.

Like so many Silicon Valley startups, Atheros can trace its roots to the engineering department at Stanford University. Professor Teresa H. Meng and Stanford's current president, John Hennessy, formed the company in 1998 to build chips capable of shuttling information across wireless spectrum.

Atheros found itself as a leader in the burgeoning market for Wi-Fi communications. That was the good news. The bad news was that Intel came to see Wi-Fi as a way to build demand for laptops running its chips. Intel started bundling Wi-Fi functionality with existing chips through its Centrino brand, undercutting Wi-Fi specialists such as Atheros in part by pouring hundreds of millions of dollars into marketing.

That looked like "it was going to kill us," said Craig H. Barratt, Atheros' CEO, during a recent interview before the acquisition was announced. "Here was the world's biggest chip company saying they would take their versions of your technology and bundle it."

An Australian-born alum of Stanford, Barratt has spent years suffering through jokes about his standing as the "lesser" Craig in the chip game. Intel's former chief executive and chairman, Craig R. Barrett, who led the company's assault on Atheros, stole much of the attention. (The ultimate indignity came when, because of a publisher's mixup, Craig Barrett started receiving royalty checks for a book penned by Craig Barratt. "He figured out the problem and sent the checks back to me," Barratt said.)

Atheros survived Intel's notoriously aggressive campaigns by staying at the cutting edge of the ever-evolving Wi-Fi technology and piggybacking on Intel's marketing heft.



CLOCKWISE FROM TOP RIGHT: DAVID NEVALA; COURTESY QUALCOMM; GETTY IMAGES

worldmags

The upstart consistently rolled out new chips offering the latest speed advances while Intel moved at the slower pace of a mammoth integrator. Intel's Centrino marketing blitz depicted, among other things, people blissfully checking e-mail from the beach. They trained consumers and hotels, coffee shops, and airports to crave Wi-Fi–and unintentionally built a bigger market for Atheros. "The irony is that Intel made Atheros in a way," Barratt says.

Intel has since pulled back from its Centrino program and turned its attention to areas such as security and graphics. Barratt sees it as a concession of sorts. "Even the biggest chip company in the world cannot afford to give away products forever," he says. Today, chips from Atheros sit inside computers from all of the major PC makers, particularly in lower-end and midrange machines.

Atheros also has ridden the latest consumer electronics wave by adding wireless functions to products ranging from **Amazon.com**'s Kindle to home routers and cell phones. In recent years, the company has started to diversify away from Wi-Fi by designing its own Bluetooth technology for short-range communications and making acquisitions in the GPS and Internet-over-powerline markets. It's part of a big bet on the so-called Internet of Things in which all manners of devices, from laptops to washing machines and even shoes, will broadcast their whereabouts and activities to the network.

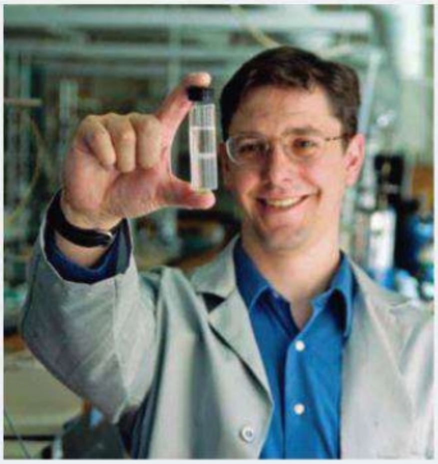
Even before the acquisition rumors, Wall Street was enthusiastic about the changes: Atheros shares surged from \$24.58 last September to \$35 earlier this month. In its third quarter, Atheros posted a 58 percent year-over-year rise in revenue to \$247.1 million.

For Qualcomm, which has also benefited as the market for smartphones exploded, Atheros is a means of expanding into new businesses. "There is not a whole lot of overlap," says Tore Svanberg, the senior chip analyst at Stifel Nicolaus Research. "All of the areas Atheros is playing in could be instrumental to Qualcomm's growth. They are very complementary."
—*Ashlee Vance with Ian King*

The bottom line *Atheros built a profitable niche with its wireless chips. Its \$3.1 billion sale to Qualcomm will help the latter expand beyond smartphones.*

Innovator

George Huber



The chemical engineer has developed a process for creating high-value chemicals out of little more than sawdust and cornstalks

In 2008 two men showed up at George W. Huber's office and flashed FBI badges. Huber, 36, a professor of chemical engineering at the University of Massachusetts Amherst, had just received a multimillion-dollar grant from the military for his biofuel research. The federal agents at his doorstep wanted to make sure no one was spying on him. "I initially mistook them for salesmen," he says.

Huber doesn't think spies are following him, but oil companies, energy experts, and investors have started paying close attention to his work. Huber has developed a process for creating benzene, toluene, and xylene (known collectively as BTX). The latter two are high-value chemicals that can be blended with gasoline to fuel autos more cleanly and cheaply. All three are also essential in the manufacture of plastics, fabrics, detergents, and countless other products. While today's BTX supply is derived from petroleum, Huber uses inexpensive, nonfood biomass such as sawdust and cornstalks to create the chemicals.

In Huber's patented conversion process, the biomass is fed into a reactor, where it is heated to 600C in the absence of oxygen. The gases emitted by the decomposing plant materials are then blended with a catalyst that forms them into carbon compounds. That catalyst is Huber's secret sauce: He won't discuss it except to say that it's composed of silica and alumina, materials as cheap as sand. The process requires no fossil fuels, so it's a greener way to produce the chemicals, says Huber. It's cheaper, too: He estimates that it would cost \$1 to \$2 to produce a gallon of benzene using his process, compared with roughly \$3.50 a gallon using petroleum.

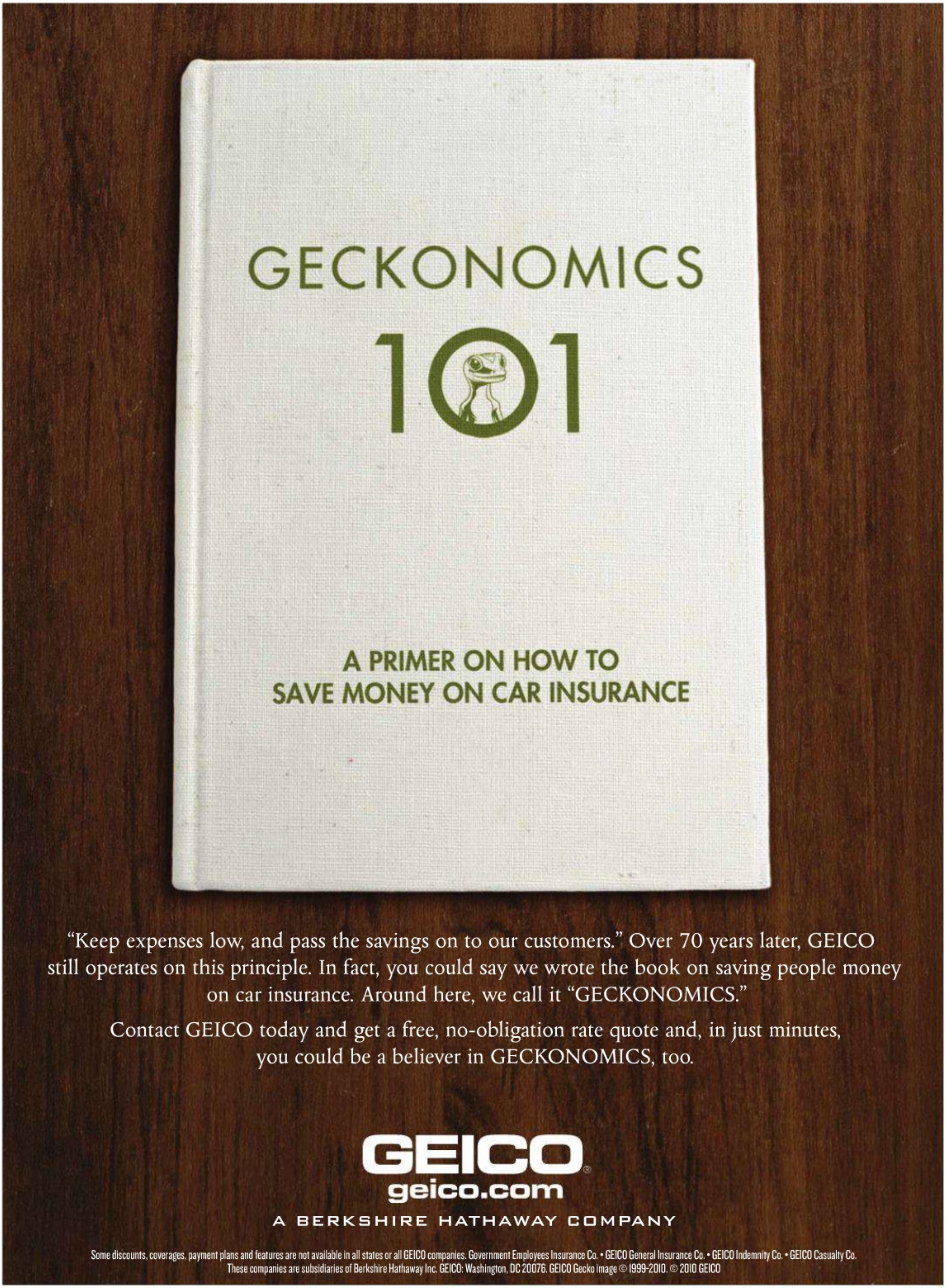
Along with entrepreneur David Sudolsky, Huber formed Anellotech to build a pilot plant to scale up his process. The startup hopes to raise \$18 million over the next year to supplement a \$4 million government grant. Eventually, Anellotech plans to license the procedure to companies so they can build their own plants. Other companies including Ensyn and UOP are racing to perfect the conversion of biomass into fuels and chemicals. Anellotech says its method is superior because it requires only a single reactor and doesn't necessitate high pressure or costly processes such as hydrotreating.

Huber holds a PhD from the University of Wisconsin-Madison. He wasn't always a good student. He failed his first chemistry test as an undergrad at Brigham Young University. "That was the wake-up call I needed," says Huber. "I ended up getting an A-minus in the class." The same year, he started studying how refineries work and got hooked. "My family laughs at me because I just love petroleum refineries," says Huber. "Most people think of them as these dirty, awful places, but I think they are beautiful, complex, highly integrated systems." Ⓑ —*Caroline Winter*

Wake-Up Call ▶ Flunked his first chemistry test at Brigham Young University

Invention ▶ A cheaper, greener way to make chemicals from biomass

Secret Sauce ▶ A catalyst made of silica and alumina



GECKONOMICS
101
A PRIMER ON HOW TO SAVE MONEY ON CAR INSURANCE
"Keep expenses low, and pass the savings on to our customers." Over 70 years later, GEICO still operates on this principle. In fact, you could say we wrote the book on saving people money on car insurance. Around here, we call it "GECKONOMICS."
Contact GEICO today and get a free, no-obligation rate quote and, in just minutes, you could be a believer in GECKONOMICS, too.
GEICO®
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A BERKSHIRE HATHAWAY COMPANY
Some discounts, coverages, payment plans and features are not available in all states or all GEICO companies. Government Employees Insurance Co. • GEICO General Insurance Co. • GEICO Indemnity Co. • GEICO Casualty Co.
These companies are subsidiaries of Berkshire Hathaway Inc. GEICO: Washington, DC 20076. GEICO Gecko image © 1999-2010. © 2010 GEICO

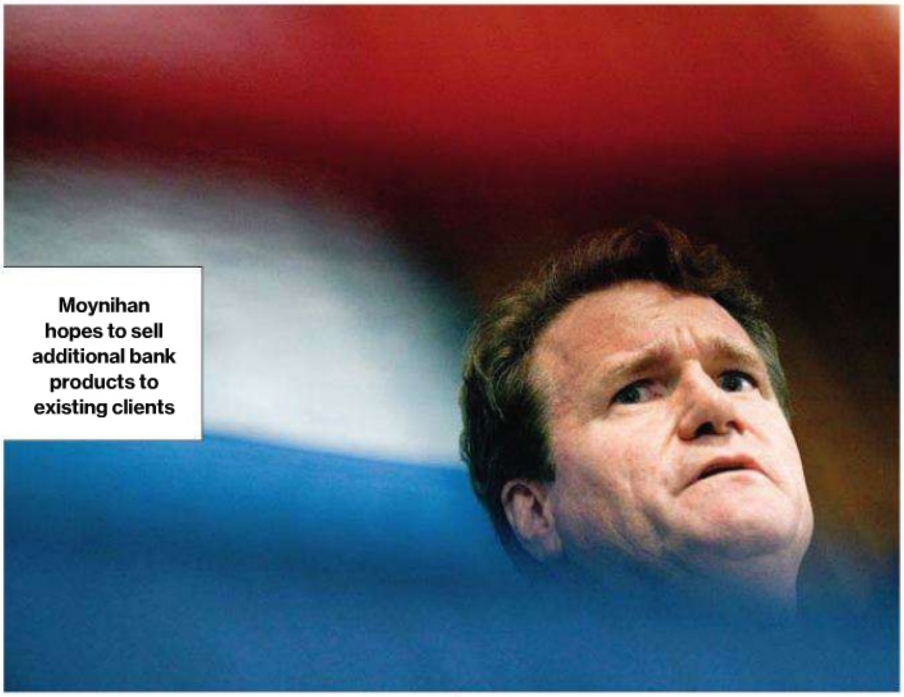
Contents ▶ Betting (again) that big companies are undervalued 40 ▶ Private equity firms look to unload 41 ▶ Lethal brew in Brazil: Fast growth, excessive consumer credit 42 ▶ A Japanese forecaster sees a six-month stock rally 43 ▶ Bid & Ask: $327 million buys a lot of shoe polish 44 ● Edited by Eric Gelman

Markets&Finance

Still Fighting Fires At Bank of America

▶ One year into the job, CEO Moynihan continues to cope with fallout from the financial crisis

▶ "I can't be successful unless the shareholders get paid and get paid well"



Moynihan hopes to sell additional bank products to existing clients

BRENDAN SMIALOWSKI/GETTY IMAGES

Brian T. Moynihan spent his first year as **Bank of America**'s chief executive officer dealing with the aftermath of the financial crisis. In 2011 he'll do more of the same. Since succeeding Kenneth D. Lewis on Jan. 1, 2010, Moynihan, 51, has struggled to stanch loan losses and forestall a surge of litigation at the biggest U.S. lender while trying to mend relations with customers, regulators, and investors.

Last month he paid $2.8 billion to government-owned companies **Fannie Mae** and **Freddie Mac** to settle claims that the bank sold them defective mortgages. It was a major step toward resolving liabilities taken on with the 2008 purchase of Countrywide Financial. "Brian's got his hands totally full," says Stephen A. Schwarzman, CEO of **Blackstone Group**, the world's biggest buyout firm. "He is in firefighter mode, dealing with fires that will be contained but need attention."

One new challenge may come from the website WikiLeaks, whose director, Julian Assange, has said he will "take down" an American bank by releasing data from an executive's hard drive early this year. While Assange hasn't named the bank, Moynihan has set up a task force led by Chief Risk Officer Bruce Thompson to prepare for the possibility, says a person with knowledge of the plan who declined to be named.

The Charlotte-based bank, with $2.3 trillion in assets, 284,000 employees, and 5,879 branches, is lagging behind **Citigroup** and other rivals in recovering from the financial crisis.

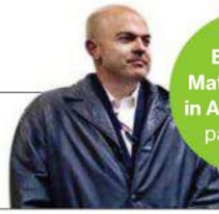
"Moynihan needs to win the confidence of the markets, which he obviously doesn't have now"

The company's shares fell 11 percent last year, the second-worst showing in the 24-company **KBW Bank Index**. Citigroup rose 43 percent. Bank of America, which repaid its $45 billion in U.S. bailout funds in 2009, traded at yearend for about 60 percent of book value. The industry average is 94 percent. The bank, which reports earnings on Jan. 21, lost $994 million in the first nine months of 2010 on revenue of $87.8 billion, compared with a $6.5 billion profit and revenue of $94.6 billion in the year-earlier period. "Moynihan needs to win the confidence of the markets, which he obviously doesn't have now," says Marty Mosby, an analyst at **Guggenheim Securities**, which owns 1.9 million Bank of America shares.

"The stock price doesn't reflect, I think, the value of the franchise or the work we've done," Moynihan said on Bloomberg Television on Dec. 10. "I can't be successful unless the shareholders get paid and get paid well."

Moynihan, who declined to comment for this story, is trying to integrate the businesses Lewis assembled through more than $130 billion in acquisitions that made Bank of America the nation's largest retail bank, debit-card issuer, and mortgage servicer. Growth will come from selling products to customers across divisions, Moynihan told 200 executives at a meeting in Charlotte in November, according to two managers who attended. Bankers will encourage retail deposit customers to use the bank's credit cards. Commercial-banking clients will be steered to financial and capital markets advisers gained through the 2009 acquisition of Merrill Lynch.

Selling across divisions has been a goal of big banks since at least the 1980s. Previous efforts haven't produced promised results. "It's



Brinkley: Matchmaking in Afghanistan page 46 ▶

been difficult to pull off in the past," says Sophie Schmitt, a Boston-based senior analyst at research firm Aite Group. "But they have all the ingredients."

Investor concerns focus on the bank's retail units, whose deposit, credit-card, and home-loan operations provide about half the company's revenue. Retail-banking profit slipped 21 percent, to $1.6 billion, through the third quarter of 2010. The firm's credit-card unit posted an $8.1 billion loss, driven by a $10.4 billion write-down related to debit-card regulation that will squeeze revenue by about $2 billion a year starting in the third quarter of this year.

In home lending, the cost of loan buybacks drove a $4 billion loss in the first three quarters of 2010, widening from $2.9 billion in the year-earlier period. The company had received demands to repurchase $21.6 billion in faulty mortgages from Fannie Mae and Freddie Mac, Bank of America said on Jan. 3. The firms were seeking to force the lender to buy back loans made with incorrect data, such as inflated incomes for borrowers. Bank of America said it paid $1.5 billion to Fannie Mae to end claims on $4 billion worth of loans. It gave $1.3 billion in cash to Freddie Mac to resolve or preclude claims on $127 billion in loans.

More losses may come from the bank's $141.6 billion in home-equity lines of credit, says Christopher Whalen, co-founder of Institutional Risk Analytics. Many borrowers who have defaulted on mortgages have stayed current on lines of credit so they can keep tapping them, he says. That's obscuring eventual losses for the bank, which may have to write down as much as $70 billion, he says. Bank of America spokesman Jerry Dubrowski says the "vast majority" of these loans are performing and charge-offs are declining.

A bright spot has been investment banking, boosted by the Merrill acquisition. Under Thomas K. Montag, the division posted $5.6 billion in net income in the first three quarters of last year, up 16 percent from the first nine months of 2009, after excluding a unit sale. Bank of America's brokerage unit, run by Sallie L. Krawcheck, earned $1.1 billion, unchanged from the year earlier.

Moynihan met with investors more than 120 times last year, according to Scott Silvestri, a bank spokesman. In contrast to Lewis, Moynihan has a rapid-fire speaking style that sometimes detracts from his message, says Nancy Bush, an analyst at NAB Research. "He's always thinking way faster than he can talk," Bush says.

Some investors view Moynihan's woes as an opportunity. Bruce Berkowitz of Fairholme Capital Management, who was named Morningstar's domestic stock-fund manager of the decade last year, bought 16.6 million Bank of America shares in the third quarter, according to regulatory filings. Ania Aldrich, a principal of Cambiar Investors, which holds more than 8 million warrants to buy Bank of America stock, says the bank's low valuation won't last as Moynihan moves into his second year: "Once you see some clarity on their issues, the market will realize this is a good, cheap stock." How long it takes to get that visibility could determine Moynihan's fate. "He still has a window to take care of these issues," says Guggenheim's Mosby. "This is the year he proves himself." —*Hugh Son*

The bottom line *Moynihan has to deal with loan losses and new government regulations as he steers Bank of America out of the financial crisis.*

6.3

BILLION DOLLARS

Estimated gain in the equity portfolio of Warren Buffett's Berkshire Hathaway in the fourth quarter as holdings in Wells Fargo and Coca-Cola rallied, according to Barclays.

DATA: BARCLAYS

Money Managers

Three Big Names Stick With Big Stocks for 2011



▶ **Large caps lagged badly last year. Can they rebound?**

▶ **A "once-in-a-lifetime opportunity" to get high-quality stocks cheap**

Jeremy Grantham, Bill Miller, and Donald Yacktman told mutual-fund investors that 2010 was the year to buy the biggest stocks. They're sticking with the prediction even after getting drubbed by most of their peers.

Stocks of small and midsize companies almost doubled the return of the Standard & Poor's 500-stock index in 2010. Large stocks rose 15 percent, compared with 27 percent for midcap stocks and 27 percent for small stocks, Bloomberg data show. Mutual funds that invest in large stocks returned 14 percent, vs. 23 percent for midcaps and 26 percent for small caps.

Big stocks lagged after Federal Reserve Chairman Ben Bernanke said in late August that the Fed would provide more stimulus. His comments triggered a rally in riskier assets, including smaller stocks. "Small stocks generally do better when you are coming out of a recession," says Michael A. Mullaney, portfolio manager at Fiduciary Trust in Boston, where he helps oversee $9.5 billion.

Still, Yacktman and the others are making the same case for the new year as they did for the last: Big companies—those with market values of roughly $10 billion or more—are undervalued compared with smaller stocks, and their earnings will benefit more from faster economic growth outside the U.S. "In 40 years, I have rarely seen a situation where so many big, profitable international companies are selling at such relatively cheap prices," says Yacktman, who manages his $2 billion **Yacktman Focused Fund** from Austin, Tex.

FROM LEFT: PHOTOGRAPH BY BENJAMIN LOWY FOR BLOOMBERG BUSINESSWEEK; GRANTHAM MAYO VAN OTTERLOO LLC/BLOOMBERG; LEGG MASON/BLOOMBERG; FRANK POLICH/BLOOMBERG NEWS; RUBBERBALL/GETTY IMAGES

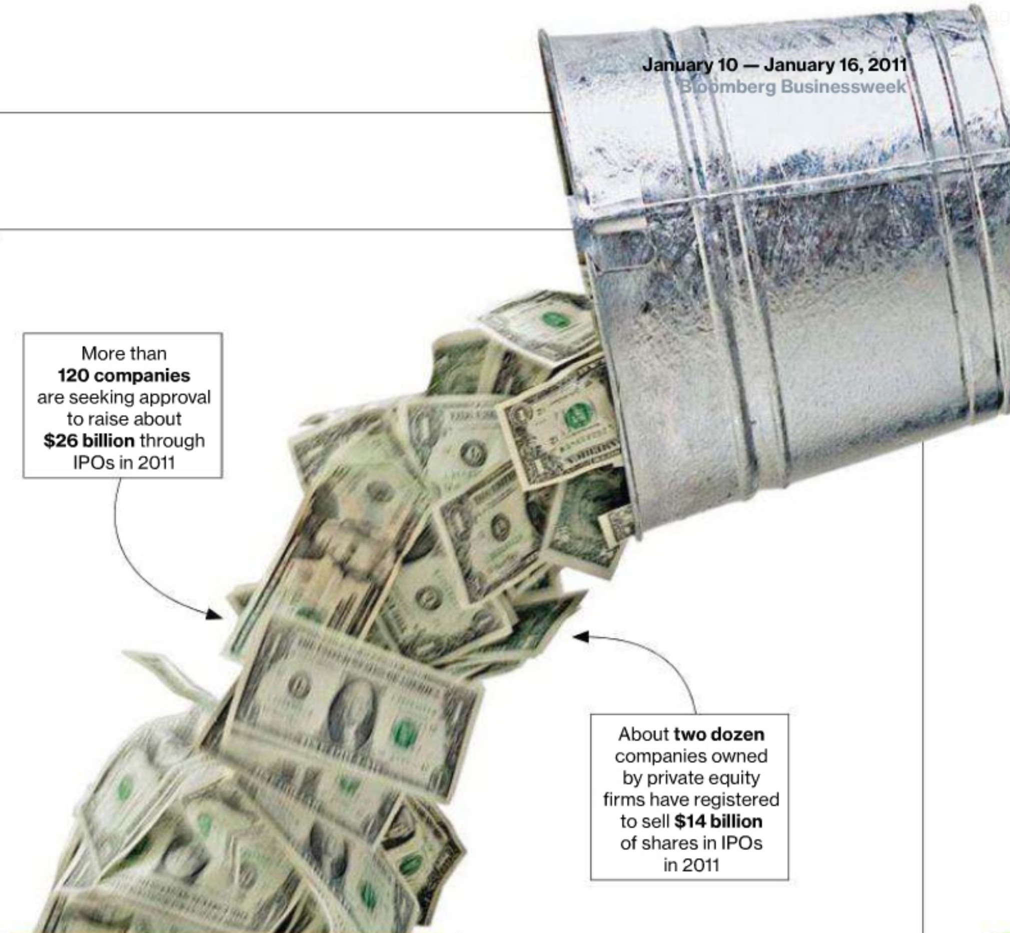
On the basis of profit, shares of larger companies are half as expensive as smaller stocks. The S&P 500, which is dominated by large companies, trades at 15.8 times reported income, while the small-cap Russell 2000's multiple is 34.4. Miller, chief investment officer of Legg Mason Capital Management, said in a July newsletter that investors have a "once-in-a-lifetime opportunity" to buy large-cap U.S. stocks at the cheapest prices in almost six decades. Known for beating the S&P 500 a record 15 straight years through 2005 at **Legg Mason Capital Management Value Trust**, Miller, 60, was behind the index for the next three years. Robert Hagstrom, another Legg Mason portfolio manager, reiterated the case for large stocks in a December report, saying they are attractively valued and have exposure to fast-growing emerging-market economies.

Yacktman, Miller, and Grantham did not fare well in 2010, even compared with other large-cap managers. Yacktman Focused trailed 79 percent of similar funds last year, according to Bloomberg data. Grantham's $14.9 billion **GMO Quality Fund** gained 5.5 percent, worse than 99 percent of its peers, even though top holding **Oracle** was up 28 percent. Two of the top five holdings in Yacktman Focused–**Microsoft** and **Pfizer**–are among its worst performers.

The $4 billion Legg Mason Capital Management Value Trust, which has **IBM** and **Amazon** among its top 10 holdings, gained 6.7 percent last year, trailing 98 percent of similarly managed funds, Bloomberg data show. Miller's midcap fund, the $2 billion **Legg Mason Capital Management Opportunity Trust,** rose 17 percent.

In November, Grantham's firm, Boston-based **Grantham, Mayo, Van Otterloo**, predicted that the highest-quality stocks will return 5.1 percent a year, adjusted for inflation, over the next seven years, compared with an annual after-inflation loss of 0.8 percent for small stocks. Grantham, the company's chief investment officer, wrote in a newsletter that he believes "high-quality stocks should have an even bigger win over low quality than our GMO numbers suggest." —*Charles Stein*

The bottom line *Three noted money managers are holding to their view that high-quality, large-cap stocks offer the best values in the market.*



Private Equity

Buyout Firms Are Set For a Selling Spree

- They hope to shed companies bought in the boom
- "This is the first big window where we can see an exit"

A wave of initial public offerings in the U.S. this year will come from companies owned by private equity firms. **KKR**, **Blackstone Group**, and **Carlyle Group** are betting that a continuing stock market rally will increase demand for some of the debt-fueled acquisitions they completed as credit markets started to freeze four years ago. "This is the first big window where we can see an exit," says Timothy Cunningham, a manager at **Thornberg Investment Management**. "Private equity funds will try to take advantage of that."

HCA Holdings, **Nielsen Holdings**, **Kinder Morgan**, and more than two dozen other companies owned by private equity firms have registered with the Securities and Exchange Commission to sell $14 billion of shares in initial offerings, or 53 percent of the amount on file, according to data compiled by Bloomberg. That total is more than double the $6.6 billion raised in 2010, when private-equity-backed IPOs accounted for 15 percent of total offerings.

Overall, more than 120 companies are seeking approval from the SEC to raise about $26 billion through IPOs. **Barclays** estimates that U.S. companies will complete as much as $50 billion of sales this year, a 34 percent increase from 2010.

Investors have reason to be wary of private-equity-backed offerings. Shares of the 31 companies brought public by private equity firms in the U.S. last year rose 3.8 percent on average in the first month of trading, less than half the 8.1 percent first-month advance for all other IPOs, data compiled by Bloomberg show. Venture-capital-backed offerings, which raised $3.2 billion, increased 7.8 percent on average.

The private-equity-backed companies scheduled to go public this year have almost twice the net debt to operating cash flow as the average private-equity-backed IPO last year. That's a concern, says Lawrence Creatura, fund manager at **Federated Investors**: "You'll have to endure the burden that most free cash flow is going towards debt service and debt pay-down."

Companies backed by venture capital firms have filed to raise $2.86 billion in IPOs, a decrease from last year's total. Venture-backed companies such as Facebook and Twitter

have shown they can raise equity capital without seeking an IPO. **Facebook** raised $500 million from **Goldman Sachs** and Russia's **Digital Sky Technologies**, according to three people familiar with the matter. **Groupon**, the daily-deal coupon site based in Chicago, raised $500 million in its latest round of financing, according to its SEC filing in late December.

Companies controlled by buyout firms face more pressure to go public both to pay back debt and to allow their owners to cash out, says Tim Loughran, a finance professor at the University of Notre Dame's Mendoza College of Business. "Facebook and companies like that can already sell equity without doing an IPO," says Loughran. "They can wait for a really good time to go public. The private equity firms have a lot of debt which forces [them] to move at a quicker pace."

—Michael Tsang and Lee Spears

The bottom line *With stocks rallying, private equity firms see a chance to sell shares of companies they bought using lots of borrowed money.*

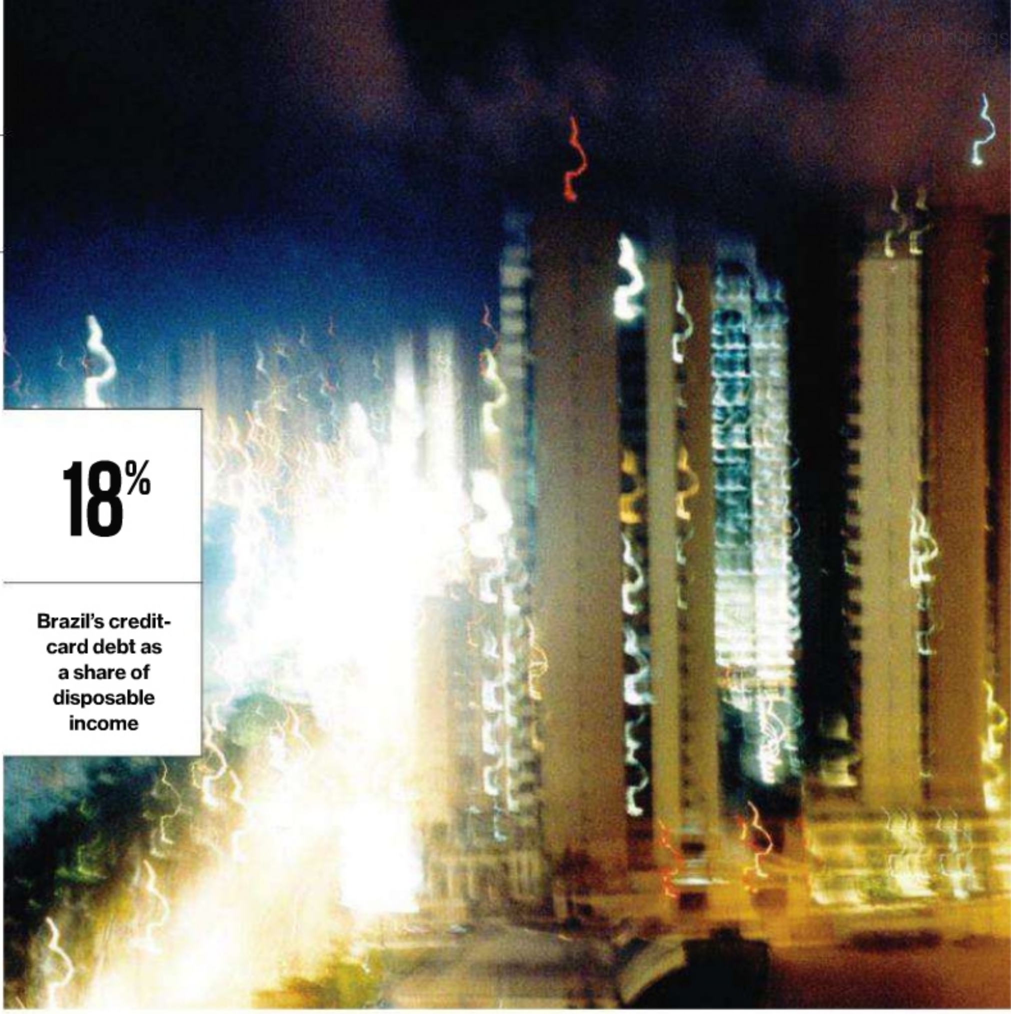
Emerging Markets

Brazil's Credit Boom Could End in Tears

▶ Consumer credit has shot up fivefold since the end of 2002

▶ "It's time to be a little careful about the B in BRIC"

The Nov. 9 rescue of Brazil's 21st-largest bank, **Banco PanAmericano**, has exposed cracks in what many had regarded as one of the most solid financial systems among emerging-market countries. Brazil's economy grew at a 8.4 percent clip in the first nine months of 2010–its fastest pace in more than 15 years–powered in part by a sharp increase in government-subsidized loans and a rapid expansion in consumer credit. That can be a lethal cocktail. The data in Brazil are troubling: Late payments on credit cards and other consumer loans jumped 23 percent in November from a year earlier, prompting government leaders to begin scaling back their easy-credit policies. "It's time to be a little bit careful about the B in BRIC," says Jim O'Neill, chairman of **Goldman Sachs Asset Management** and the man who coined the BRIC acronym for Brazil, Russia, India, and China.



18%

Brazil's credit-card debt as a share of disposable income

MAT JACOB/TENDANCE FLOUE

Former President Luiz Inácio Lula da Silva, a founder of Brazil's Workers' Party, impressed Wall Street with his commitment to free-market policies. Yet even he was unable to resist the temptation of indulging in an age-old Brazilian tradition: the election-year splurge. The national development bank, known as BNDES, made $101.1 billion in loans in the 12 months to October, a 33 percent increase from the same period a year earlier. Lula's protégée and successor, Dilma Rousseff, pledged to rein in spending as she assumed power on Jan. 1.

Bankers in New York, London, and as far away as Shanghai have a lot riding on how well Rousseff steers Latin America's biggest economy. With interest rates at all-time lows in much of the developed world, the 12 percent return on benchmark 10-year Brazilian government bonds has attracted money from all over. Foreign investors poured $15.9 billion into Brazil's stock market in the past two years. "The quest for yield and higher investment returns has flooded Brazil and other emerging markets with capital from around the world," says Russell Certo, a managing director at New York-based investment bank Gleacher & Co.

The capital inflows have buoyed Brazil's currency, the real, causing it to rise 34 percent against the dollar since late 2008. Finance Minister Guido Mantega, a holdover from the previous administration, has said he would consider a number of measures, including the imposition of new capital controls to fight the currency's appreciation, which puts Brazilian exporters at a disadvantage.

At the same time, Brazil's central bank is moving to curb the growth in consumer loans. The country has witnessed a fivefold expansion in consumer credit over the past eight years, with the total value of outstanding loans reaching $440 billion in October, according to central bank figures. This explosion was triggered in part by a 2001 regulatory change that allowed lenders to package auto, payroll, and other consumer loans into securities called FIDCs. The market for such notes has grown from nearly $290 million in 2003 to more than $35 billion last year.

Big Brazilian banks have stopped buying the credit portfolios since a November government probe into PanAmericano revealed losses stemming from improper accounting of sales of its loans. "PanAmericano was the wake-up call," says Denise Debiasi, the São Paulo -based managing director for Latin America at FTI Consulting, a Baltimore



firm that advises on compliance, risk, and finance. "There's risks people may be overlooking—like credit quality—as the market booms." PanAmericano won't comment on the ongoing investigations, according to a spokesman at the bank's public relations firm.

To head off a subprime-style crisis, Brazilian authorities in December upped reserve requirements on time deposits held by banks to 20 percent from 15 percent. Banks must put aside more capital to back consumer loans whose terms exceed 24 months.

The government is also looking to regulate Brazil's credit-card industry. There are now 153.4 million credit cards in circulation in the country, triple the number from 2003. The average debt load of Brazilian consumers amounts to 18 percent of total disposable income, compared with 13 percent in the U.S., says Morgan Stanley. In a Nov. 30 interview, Henrique Meirelles, who at the time was Brazil's central bank chief, indicated that a special task force would be convened to study the industry. "Some supervision could be proper," he said. "The case of PanAmericano showed how important this is."

—*Alexander Ragir and Dawn Kopecki*

The bottom line *The bailout of a Brazilian lender has exposed the need for greater supervision of the local consumer credit industry, which is growing rapidly.*

Asian Markets

Seeing a Surge in Japanese Equities

▶ **Kathy Matsui says stocks will climb 18 percent in six months, then drop**

▶ **Don't get "too emotionally hung up on Japan's structural problems"**

The only strategist to predict the rally and subsequent decline in Japanese stocks last year now says the Topix index will climb 18 percent in the next six months. Kathy Matsui, chief Japan equity strategist for **Goldman Sachs** in Tokyo, is telling clients to buy automakers and technology producers because profits will rise as the yen retreats against the dollar.

Matsui is bullish even after confidence among the nation's largest manufacturers fell for the first time since March 2009, as unemployment climbed and executives' reluctance to invest pushed cash reserves to an all-time high. "Many investors make the mistake of becoming too emotionally hung up on Japan's structural problems, and therefore they miss the cyclical opportunities," says Matsui, 45. Japanese stocks rallied 39 percent from March to August 2009, for example. "If you have the stars aligned with a better U.S. economy, a weaker yen, earnings going back to 2007 peaks, and very underweight foreign investors," she says, "that could easily deliver 15 to 20 percent."

In a year when forecasters in Japan were wrong by an average of 21 percentage points, Matsui's December 2009 projection that the Topix would rise to 1050 in the first half of 2010 then fall to 800 stood out. The index advanced 10 percent, to 998.90, by Apr. 15, then retreated 20 percent, to 803.12, on Nov. 2.

Her forecast for 2011 follows a similar pattern. The index of 1,663 Japanese companies will rise 20 percent, to 1080, in the next six months, she says.

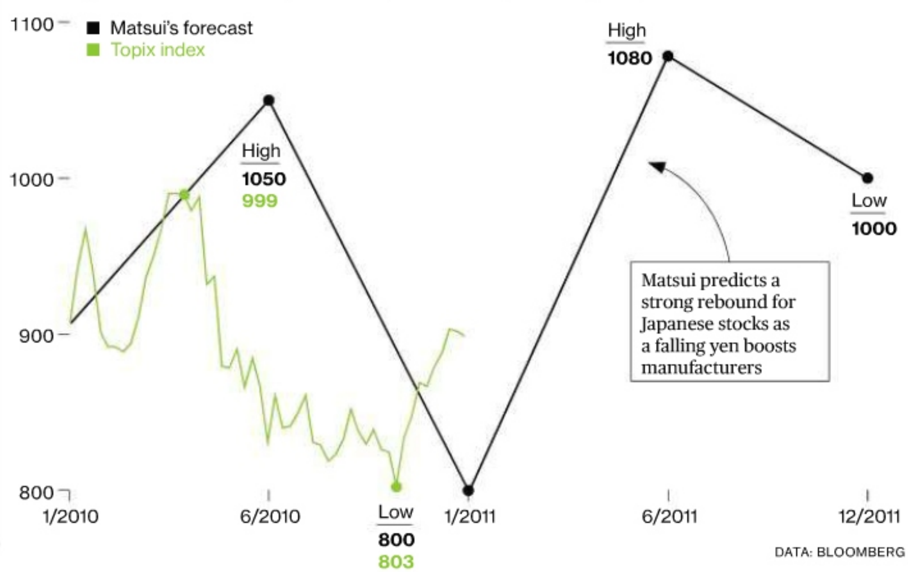


Matsui likes companies that do a lot of business in the U.S.

One reason is that the yen will decline against the dollar as economic growth in the U.S. picks up. A weaker yen helps Japanese manufacturers by making their products more affordable around the world. On Nov. 1 the yen hit 80.22 to the dollar, the strongest level since April 1995. By Jan. 4 the yen had fallen 2.2 percent, to 82.06. For every one-yen decrease vs. the dollar, companies in the Nomura 400-stock index gain 0.5 percent of their recurring profit, according to Takashi Ito, a strategist at Nomura Securities. He

A Predictable Pattern for Japan's Topix Index?

Goldman Sachs' Matsui, the most accurate stock-market forecaster in Japan last year, sees stocks following a similar rise-and-fall path in 2011, with the Topix ending the year at 1000.



DATA: BLOOMBERG

said income at automakers and software developers will benefit the most, rising 2.5 percent and 2.3 percent, respectively, for every one-yen decline.

The index will slump to 1000 in the second half of the year, Matsui says. She expects investors to shift money to faster-growing Asian markets such as China once policymakers in those nations curb inflation.

The average forecast from strategists at eight banks surveyed by Bloomberg, including **Morgan Stanley** and **Credit Suisse Group**, was for Japanese stocks to gain 20 percent last year. The index instead slumped 1 percent as the yen surged 15 percent against the dollar, cutting the value of profits for Japan's exporters. Strategists forecast the country's shares will advance 15 percent in 2011, based on the average estimate from nine banks tracked by Bloomberg.

Byron Wien, the **Blackstone Advisory Services** vice-chairman who called Japan stocks one of the best bets for 2010 last January, says he's "neutral" after Bank of Japan policies to stimulate economic growth failed to reverse 20 months of deflation. "I have been disappointed by Japan," says Wien. Matsui, a California native and Harvard graduate who first visited Japan on a scholarship to Kobe University in 1986, favors companies with the highest proportion of U.S. sales. **Nikon** and **Bridgestone** are among 31 stocks she likes because they may benefit from American shoppers buying more cars, computers, and cameras.

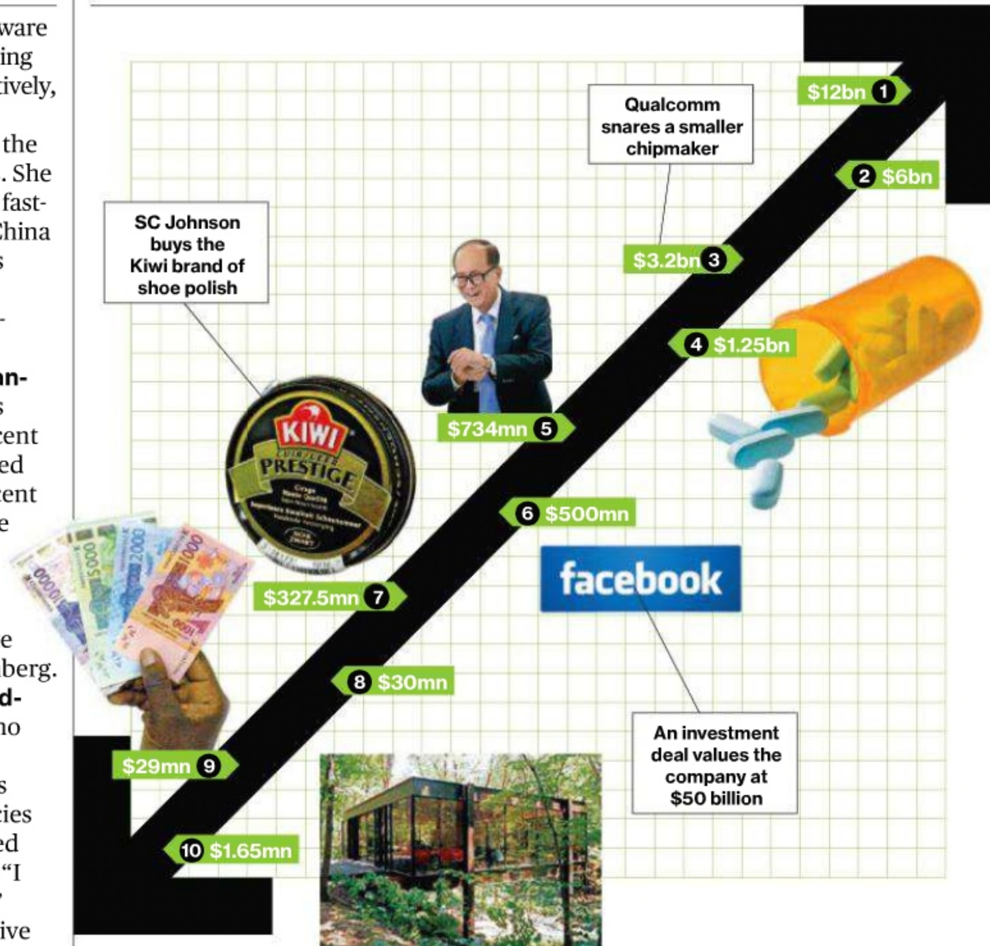
Nikon, which gets more than 30 percent of its revenue from North America, rose 15 percent from Nov. 1 to Jan. 4. Shares advanced even after the Tokyo-based maker of cameras and lenses reduced its annual profit forecast on Nov. 4. Bridgestone, the world's largest tiremaker, gained 13 percent. The Tokyo-based company, which got 43 percent of its revenue from North and South America last year, rose amid record rubber prices. "Japan has a way of having these short spurts of outperformance," says Matsui. "If you don't catch the wave quickly, you can miss it."

—*Lynn Thomasson and Anna Kitanaka*

The bottom line *While Japan's economy remains troubled, Matsui says stocks will rally strongly in the next six months thanks in part to the weaker yen.*

Bid & Ask

by Cristina Lindblad



1 **Chile's central bank** has earmarked $12 billion for dollar purchases to fight appreciation of the peso.

2 **General Electric Capital**, GE's finance arm, sold $6 billion worth of bonds, marking the biggest U.S. corporate bond offering in 11 months.

3 **Qualcomm**, the world's largest maker of mobile-phone chips, is acquiring Atheros Communications, a California maker of Wi-Fi networking equipment, for $3.2 billion.

4 **CVS Caremark,** the No. 1 provider of prescription drugs in the U.S., agreed to buy Universal American's Medicare Part D unit, which serves some 1.9 million customers, for $1.25 billion.

5 **Hutchison Whampoa,** the company controlled by billionaire Li Ka-shing, paid $734 million for a bundle of Hong Kong assets that includes shares in a container terminal operator and a stake in a building in the city's Kowloon district.

6 **Facebook** received a $500 million investment from Goldman Sachs and Digital Sky Technologies in a deal that values the social-networking site at $50 billion.

7 **Sara Lee** is selling its shoe-care business, which includes the Kiwi brand, to SC Johnson for $327.5 million.

8 Liberty Media Chairman **John Malone** donated $30 million to Johns Hopkins University, his alma mater.

9 **Ivory Coast** missed a $29 million bond payment due on Dec. 31 amid a fight for political control of the West African nation. The country has until the end of the month to pay up before it will be declared in default.

10 A midcentury modern house in Highland Park, Ill., has been listed for $1.65 million by a **Sotheby's** affiliate. A scene from the movie *Ferris Bueller's Day Off* shows the home's glass garage being totaled by a Ferrari. **B**

CLOCKWISE FROM LEFT: SEYLLOU/AFP/GETTY IMAGES; DENIS/REA/REDUX; JEROME FAVRE/BLOOMBERG; FRAREDAVIS PHOTOGRAPHY/GETTY IMAGES; ANTOINE ANTONIOL/BLOOMBERG; SUDLER SOTHEBY'S REALTY

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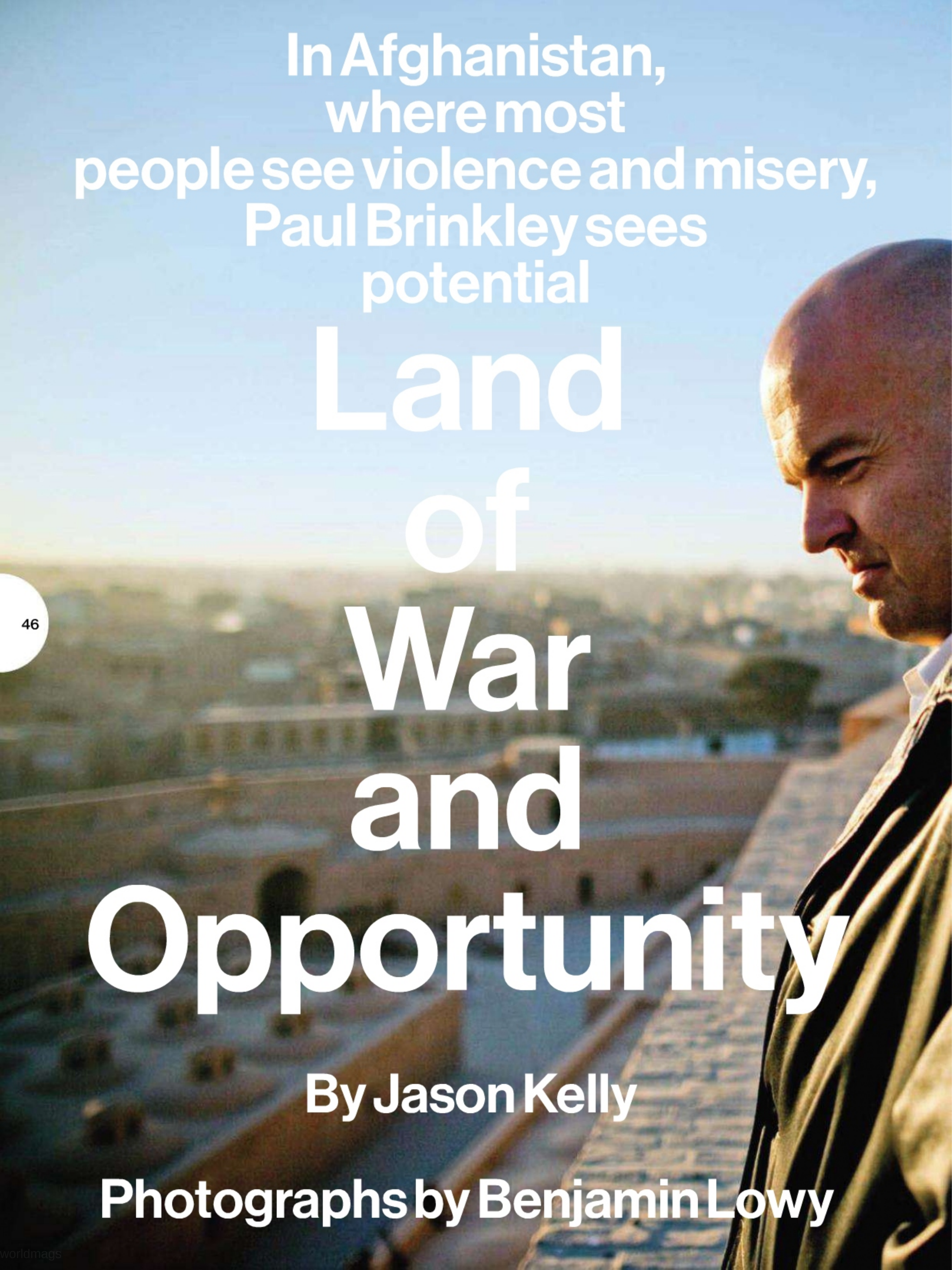


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In Afghanistan, where most people see violence and misery, Paul Brinkley sees potential

Land of War and Opportunity

By Jason Kelly

Photographs by Benjamin Lowy

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Brinkley atop the 700-year-old Qala Ikhtyaruddin

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Herat: One of Brinkley's biggest success stories

The skyline of the city of Herat, in the westernmost corner of Afghanistan, is dominated by the Qala Ikhtyaruddin, a 700-year-old stone citadel. On a chilly December afternoon, as the sun begins to dip, the citadel's grounds are largely unoccupied. The general public isn't allowed in until renovations to the time-ravaged site are finished. Paid for in part by a $725,000 grant from the U.S. government, the project is scheduled to be completed at the end of 2011.

Paul A. Brinkley isn't the general public. As U.S. Deputy Under Secretary for Defense, he moves freely behind the barricades, ushering a handful of American visitors, including Silicon Valley executives Atul Vashistha and Mike Faith, the heads of Neo Group and Headsets.com, through dark corridors and up steep stairways to the highest reaches of the fortress. The tour comes after a morning of meetings with the provincial governor and the local university's chancellor and students, all of them pushing, along with Brinkley, for the executives to consider a noble and dangerous proposition: opening up shop in Afghanistan. "I've never regretted taking a businessperson to the theater," Brinkley says. "This is about getting their eyes on the problem."

In Herat, Kabul, and cities large and small, Brinkley serves as tour guide, ambassador, fixer, motivational speaker, and leader of the unofficial Afghanistan chamber of commerce. With all of his titles and duties, he prefers to think of himself primarily as a matchmaker, negotiating high-stakes unions between multinational companies like IBM and JPMorgan Chase and Afghan officials and entrepreneurs. Building a culture of business is the only way Brinkley and General David Petraeus, commander of NATO forces in Afghanistan, believe they can counteract the legendary forces of destruction here—from decades of war and deprivation to the brutal rule of the Taliban and a reliance on opium as a chief export. "It's an infusion of optimism in what can seem like a hopeless situation," Brinkley says. "The Afghans say, 'People actually want to do business with us? Maybe there is something at the end of the rainbow.'"

The Task Force for Business & Stability Operations was launched in 2006 as part of the Defense Dept.'s effort to link military strategy and economic development in Iraq. For four years the task force recruited Western companies in an attempt to modernize Iraq's banking system and reopen factories. Early results were unsuccessful. Security concerns prevented staff from restarting most heavy manufacturing sites, and overseas companies balked at doing business in Iraq because of the very real possibility that their employees could be wounded or killed. A former chief information officer at JDS Uniphase in California, Brinkley joined the Defense Dept. to help with internal business operations. His work in Iraq spurred the creation of the task force. "When we started our work in May 2006," he says, "[Iraq] was in a complete daily deterioration."

The task force ultimately sponsored more than 200 visits by corporate executives and investors, including Honeywell International Chief Executive Officer David M. Cote and Boeing CEO James W. McNerney Jr., which generated investment commitments of more than $5 billion, according to task force data.

That doesn't include oil-related investments; Iraq, home to the world's fifth-biggest oil reserves, has, finally, seen some success in reconstructing its energy industry. On Jan. 3 the country agreed to build pipelines across its shared border with Jordan. "The idea of what the military is trying to do is a constructive one," says Isobel Coleman, a senior fellow at the Council on Foreign Relations. "If you're there for the long haul, creating jobs and sustainable businesses is crucial."

With the Iraq project coming to an end, Brinkley shifted his focus in 2010 to Afghanistan, an even more daunting task. More than 30 years of economic and political distress dating to the Soviet invasion of 1979, and spanning the Taliban era and nearly a decade of war, have turned the country into a synonym for hopelessness. Corruption is rampant—accusations reach all the way up to President Hamid Karzai's family—and unlike Iraq, Afghanistan didn't have much of an economic base to begin with: Afghanistan's gross domestic product in 2009 was $26.9 billion, ranking it 110th in the world. Iraq

"If there's money to be made on a risk-adjusted basis, they're going to do it. Having a nice dog and pony show is not going to change the calculus."

Isobel Coleman, senior fellow at the Council on Foreign Relations

is 65th, with a GDP of $109.9 billion, according to the CIA World Factbook.

In Iraq, thanks in part to Brinkley's efforts, General Electric is building power plants to meet the country's power shortages; Honeywell opened an office last year to sell equipment to the oil and gas industry; and Daimler, having created a motor vehicle training workshop in 2008, established a Baghdad office a year later. "Success depends on those iconic companies," Brinkley says. "You augment them with mid-tier companies who are more risk-oriented. Your agility and speed comes from there." Brinkley needs to replicate and expand on the process in Afghanistan, using the military's own spending power to promote local companies and convincing multinationals that Afghanistan is not just a safe place but also a land of real opportunity.

Brinkley and his team allowed a *Bloomberg Businessweek* reporter to shadow them for five days in December as they went about their Red Bull-fueled, stubbornly optimistic work. Arriving in Kabul on a commercial flight, the task force team and one of two business delegations in the country at the time spent a day in the capital before flying to Herat, then back to Kabul for three more days of tours and meetings. From the natural resources buried in the mountains and valleys where blood is still shed almost daily, to the women-run workshops tucked in corners of Kabul, to the restless students unwilling to become another lost generation, Brinkley sees huge potential. Whether he can convince anyone it's worth the risk is another matter.

With his shaved head, tieless suit, and black leather jacket, Brinkley cuts a distinctly non-Afghan figure. He peppers his conversations with simple phrases such as "*Tashakor*" (thank you) and frequently puts his right hand over his heart, an Afghan gesture of respect. In meetings, he listens more than he speaks, usually making introductions and then retreating with a self-effacing remark. During an encounter with Herat University's chancellor, he introduces Vashistha and Faith, plugs their Silicon Valley credentials, and then says, "That's my entire contribution, so I'm going to step back."

Brinkley, 44, grew up outside Dallas and earned undergraduate and master's degrees in engineering from Texas A&M University. He is now known, to members of the task force, as "Mr. Brinkley" or "the boss."

Brinkley's pitch to executives starts at home. In the months before the December trip he was in San Francisco, Los Angeles, Dallas, Houston, and New York—and working the phones in between from his Pentagon office—to make his case. Like any good salesman, he believes that if he can just get the customer onto the showroom floor, he can close a deal. "We tap into something," says Brinkley. "There is a huge desire to support the mission among all Americans. People want to help and are at least willing to take a look at it. We just tell them, 'Come over and see for yourself.' "

Once the executives are in the country, Brinkley the matchmaker emerges. Between meetings one day in Kabul, Brinkley mentions the similarities between his job and eHarmony, a website that uses technology to figure out which singles will make the best married couples—only instead of producing children, these partnerships are meant to nurture Afghan industries and generate profits for both parents. Like any good coupling, what comes of it isn't ultimately up to the person who made the introduction. "If there's money to be made on a risk-adjusted basis that makes American CEOs comfortable, they're going to do it," says the Council on Foreign Relations' Coleman. "Having a nice dog and pony show may speed that process, but it's not going to change the calculus."

In Afghanistan, Brinkley has assembled a 75-person team with a $150 million annual budget. The group is culled from his own business network, other parts of the government, political campaigns, and nongovernmental organizations. The apparent camaraderie between its members stems from the nomadic circumstances of the job. Stretches of typical Pentagon life back in Washington alternate with long visits to a country where the mood can swing from uneasy to scary, depending on the day and location. "We live where we work," Brinkley says. "You get to know aspects of people you normally wouldn't see."

The task force's work in Afghanistan consists largely of an endless stream of meetings, many of which are conducted over platters of nuts and raisins and cups of green tea. Sleep is elusive. That owes in part to the brutality of time zones: Just as a Kabul workday ends, Washington and New York, nine and a half hours behind, are getting started. A second workday essentially begins after dinner, with BlackBerrys buzzing throughout the

One student at Herat University says "the next generation will be different if we have peace"

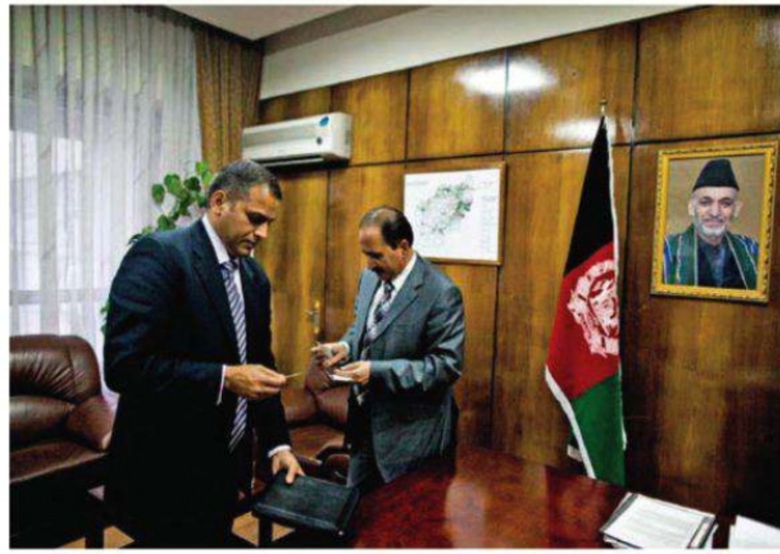


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Mobile phones are everywhere in Kabul

Atul Vashistha and Communications Minister Sangin



evening. There's no delineation between weekday and weekend, especially given that the Afghan weekend falls on Friday and Saturday. Clothing retailer kate spade new york's chief merchandising officer, Sydney Price, arrived on a Saturday, had what amounted to a working dinner with the task force, and then started Sunday morning with meetings and tours. Brinkley and his staff use their proximity to the guests for the soft sell, talking about what they saw that day, sharing stories aimed at emphasizing the country's humanity.

Security concerns mandate meticulous planning. Over the course of a two-week period, Wall Street bankers, Silicon Valley executives, and Los Angeles-based investors were ferried around Kabul and other parts of the country in armored vehicles for meetings with local business owners, artisans, government officials, and students. To deal with the unpredictability of airline schedules and traffic, team members and visitors often leave their quarters before dawn. Most meals are taken inside the compound; occasionally they are at a hotel restaurant. "I expected it to be a lot more chaotic," says Vashistha. "What I saw was much more of a high-security zone than a war zone."

The Brinkley team typically isn't embedded with the military, which allows them more freedom to work with a range of officials and executives. The group is closely connected to the military mission, though, and Brinkley is exuberant in his loyalty to Petraeus. "He has a phenomenal intellectual range and capacity," Brinkley says of the general. "We're in tight partnership."

Over the course of three December days, Petraeus meets with two separate delegations, including Vashistha's, and has a separate briefing with Brinkley. The general is appreciative of the visitors' curiosity about Afghanistan—and quick to press them to move beyond interest and into commitment. "Just like you can't commute to a fight, you can't commute to business," Petraeus says. When one member of a delegation says the task force has provided a keyhole into what's happening here, Petraeus responds: "We need you to do more than look through the keyhole. We need you to go through the door."

Kabul's infrastructure was designed for about half a million people. The city currently has a population of more than 3 million. Traffic barely moves, and the crumbling roads and bridges are constant reminders that it will take decades before Kabul joins the ranks of modern cities.

Yet flashes of 21st century life are evident. Mobile phones, sold by five different carriers, are everywhere. Afghanistan, with a population of 29 million, boasts 15 million wireless subscribers. This gives hope to outside investors that there's a technological backbone to exploit. "My cell service is better here than in the Bay Area," says Faith of Headsets.com, part of the Silicon Valley delegation. He's a colleague of Vashistha's through their local chapter of the Young President's Organization. Faith says Afghanistan's not yet a big enough market for his company, but he's surprised by the progress he sees. "I'm excited about the possibilities."

Brinkley and his visitors troop up several flights of stairs to visit with Amir Zai Sangin, the government's Minister of Communications and Information Technology, who has the enviable job of proselytizing for what is arguably the most advanced sector of the Afghan economy. An Afghan flag sits in a corner of his wood-paneled office, a large portrait of Karzai hangs behind his desk. Over juice, tea, and cookies, Sangin recounts how Afghanistan created a communications infrastructure from nothing in 2002. "People had to travel to another country to make a phone call," he says. "Now, in Kabul, even the poorest have mobile phones. The beggars have mobile phones."

There are five major telecommunications companies and dozens of domestic

"You can't commute to business. We need you to do more than look through the keyhole. We need you to go through the door."

General David Patraeus

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Vashistha meeting with future entrepreneurs

Internet service providers. About 80 percent of the population is covered by the telecom infrastructure–a bigger portion than in India, he says. "Our strategy for the last five years was infrastructure. The next five is applications."

While Afghans have been busy talking on their phones, their banking system lay fallow. Historically, Afghans have tended not to trust banks and have avoided using them. When money needed to be moved, transfer agents called *hawalas* were called in. The notion of a bank as an institution that secures savings and lends out money is still quite alien.

Nadia Dawood, an Iraqi-American, left her job on Wall Street six years ago and started working with the U.S. Agency for International Development. Eventually she landed alongside Brinkley and was charged with trying to build a modern banking system in Iraq. Saddam Hussein's government had set up a network that drove all funds through state-owned and -controlled financial institutions. The task force automated the banking sector and helped install modern services at more than 200 bank branches throughout the country. Like the rest of the task force's members, Dawood has turned her attention to Afghanistan, where among the first orders of business was persuading the government to pay its soldiers and police officers through electronic funds transfers. By the end of last year all of the military and 80 percent of the police were paid on that basis. The next step was persuading them to actually leave their money in a bank.

What the banks were–and where they were–was a question not easily answered when Dawood arrived in February 2010. Now she has a spreadsheet detailing banks' deposits and the number of branches. Getting that data was crucial for the next stage–bringing in a global financial-services company that would connect Afghanistan's monetary system to the rest of the world.

The first bank the team approached was Citigroup, which had played a similar role in Iraq. The financial conglomerate was a natural choice, given that it processes the U.S. government's payments abroad and has shown an appetite for working in emerging markets. Still, the work was neither fast nor easy. Citigroup conducted six months of due diligence in Afghanistan, including a weeklong road show with executives at the country's handful of domestic banks. The company made a deal with Afghanistan International Bank, and now the two are helping process payments made by NATO forces to local contractors. "By paying invoices in local currency, it ensures the money stays in the country to stimulate the economy," says Kevin Fitzgerald, the head of Citigroup's public-sector unit in North America, who oversees the company's contracts with the U.S. government. "The entire amount is deposited directly in a bank without being diverted or delayed by a local government agency."

Progress in Afghanistan is never linear. While the implementation of a modern banking system has shown promise, Kabul Bank, one of the country's largest institutions, was beset by a corruption scandal in 2010. Last summer six private security guards were also poisoned and stabbed at a Kabul bank branch in Mazar-e Sharif. Nothing is easy.

Noorullah Delawari, who returned to his native Afghanistan in 2002 after a career spent mostly in Southern California, where he worked at Lloyds Bank's operations there, is one of those pushing to improve the financial system. After a stretch running Afghanistan's central bank, he's now an adviser to Karzai and serves as president of the Afghanistan Investment Support Agency, whose motto is "the Silk Road to Opportunities." AISA is one of the task force's many partners, organizing road shows and pitching businesses in China, Washington, and India. During a meeting in his office with one of the task force's delegations, Delawari rattles off statistics: Through August 2010, 3,267 companies were established in the country, with 38,000 new jobs tied to the



Brinkley alternates between a Pentagon office and leading delegations to Afghanistan



Petraeus talks up the virtues of Afghanistan

investment. "Any positive development will help end this vicious war."

As Delawari speaks, Brinkley sweeps in, straight from the airport. The men embrace. "One of the pleasant surprises coming to Afghanistan was AISA," Brinkley tells the group. "It's like a massive accelerant." At the end of the meeting, Delawari insists that Brinkley accept a small carpet sample, produced at a new factory that AISA and the task force worked to get started, as a gift.

Corruption is often cited, alongside security concerns and lack of infrastructure, as one of the biggest obstacles for companies considering expansion to Afghanistan. Brinkley says the task force seeks to soothe fears about corruption by embedding accountants and legal advisers within government ministries. Ultimately, avoiding corruption is up to the companies. "It's a huge problem," says Erik Malmstrom, co-author of a November study sponsored by the Kauffman Foundation on private-sector development in Afghanistan. The report, titled "Afghanistan's Willing Entrepreneurs" and written with Jake Cusack, found something that surprises many visitors: Afghans worry less about physical threats than about the integrity of the business environment. "Every step of the way," Malmstrom says, "businesses are having to deal with corruption."

Herat is the site of some of Brinkley's most successful matchmaking, and it's easy to see why. Located about 50 miles from the relative calm of Iran—which, despite its political saber-rattling, is home to the world's 19th-biggest economy—Herat doesn't feel like a city in a war zone. Its governor, Sayed Hussain Anwari, stresses the quietude during an enthusiastic sales pitch over a breakfast of traditional breads and pan-fried eggs served with chilies at his mansion near the center of town. "People here want to keep their comfortable life. In the south, they have nothing to lose, so they fight," the governor, dressed in a business suit, explains. "Here, they have something to lose, so they don't fight." He tells the Americans that he's looking to Bangalore as a model for Herat, an analog that will be repeated throughout the day. Jobs are the top priority for both the task force and the locals. "These are hotheaded people who want to do something," Bijan R. Kian, a director of the Export-Import Bank of the United States who is Iranian-born, says of the Afghans.

Beyond the heavily guarded gates of Herat University, the male and female students who roam the dusty campus, some dressed in full burkas, agree. Inside a computer lab with rows of Lenovo machines, a group of students in the university's two-year-old computer programming school nervously show off their projects to Brinkley and his contingent. The Herat IT program got a boost in November when IBM signed a letter of intent with the University pledging to help train students after sending executives on one of Brinkley's tours. On this visit, Brinkley is trying to augment that. After the presentations, Neo Group's Vashistha offers to hire several of the students as interns. He also encourages them to look for ways to make money on what they've already created as student projects. He spends most of the afternoon and evening counseling and cajoling a smaller group of students. Ultimately, he decides that he'll start by bringing two of the students on as contractors to one of his companies; they'll work remotely from Herat. In addition, he plans to make an investment in a startup software company, Citadel Software, that he encountered during the trip.

The students respond with cautious excitement. Their lives have been split between Taliban rule and a war that began almost a decade ago. "Every day, we want something better," Eleena Kakar, a 21-year-old who recently graduated from Herat's IT program, says after a task force-hosted dinner. "The next generation will be different if we have peace, and if we get to do what we want."

Kate spade wanted to work in Afghanistan as the next step in its three-year-old partnership with the Washington-based NGO Women for Women International, a project that has taken the company to Bosnia. Brinkley's team coordinated a visit last August for kate spade executives including CEO Craig Leavitt, who announced the company's plans at an event held at the U.S. Embassy. "I was very skeptical," Leavitt says in an interview from his New York office. "We knew of the logistical problems because of the instability."

Four months later, kate spade's chief merchandising officer, Price, is reconnecting with the staff at Turquoise Mountain, a Kabul-based nonprofit that was created in 2006 through an agreement between Karzai and Britain's Prince Charles, with the goal of reviving arts and architecture in Kabul and creating an Afghan craft industry that could thrive locally and abroad. Turquoise Mountain takes 45 new students a year (970 applied in 2010) and trains them in traditional crafts. They spend about 60 percent of their time learning a spe-

Kate spade's Sydney Price investigates the wares



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Woodworking at Kabul's Turquoise Mountain

cialty, such as jewelry making, and the rest studying business, law, and technology to help them become well-rounded entrepreneurs. At a recent local exhibit the students sold $20,000 worth of goods in four hours, all to local buyers, according to Shoshana Coburn, the group's managing director.

If all goes according to plan, Afghanistan-made cashmere scarves may begin production in Kabul this year and will eventually appear in kate spade stores as part of its "hand in hand" line, alongside pom-pom scarves and other products made in Bosnia. Kate spade's approach to the products is different from the traditional "a portion of the proceeds" model. The company buys the goods outright from the workers, typically at a multiple of local market prices. Kate spade then handles all the exporting and marketing costs involved in getting it to its stores.

The advantages for the producers–in this case, Afghan women–are clear. They get the money once they produce the wares instead of waiting for their share of the sale to make its way back to them. If the products sell well, then kate spade will make additional orders. The company aims to employ upwards of 1,500 women in Kabul by the end of 2013. "The Afghans feel that any attempts by the Americans to really change anything would be half done without leaving a viable economy behind," Leavitt says.

During his August visit, Leavitt arrived at Women for Women's Kabul training institute and sat on the floor among the participants and asked how he could help. A woman who had been unable to leave her home for seven years summed it up. "She just needed a market to sell," Leavitt says.

Kate spade is perfectly suited to working in Afghanistan. "Hand in hand" is equal parts philanthropy, entrepreneurship, and branding. "This is not a cash-aid partnership," Leavitt says. "Our goal is that this is ultimately a profit center for the women and for us. This is meant to be good solid economics for everyone." Still, it'll take a lot of kate spades to make Afghanistan matter in the global economy.

What Brinkley's project really needs is scale, and natural resources are the fastest way to push the country forward. According to a June Defense Dept. study, the estimated gold, copper, and iron ore reserves in the hills of Afghanistan make up a potential trillion-dollar opportunity. (The country's Ministry of Mines thinks it could be more than $3 trillion.) It's not worth much if it stays in the ground.

The biggest single foreign investment came from mining–and from a Chinese company. Metallurgical Corp. of China was awarded the Aynak copper mine project in 2007. The Minister of Mines has held additional talks with foreign companies including ArcelorMittal, Total, and Eni, he told investors at a briefing in London last year.

Getting companies from countries not directly involved in the military effort is crucial to the long-term success of economic development, says Thomas P.M. Barnett, chief analyst at consulting firm Wikistrat. "The guys who are going to benefit are going to be from the non-Allied pool." Brinkley is agnostic and has recruited foreign companies, including Daimler, into Iraq. "This is not just about U.S. companies," he says.

Another small mine project stands as a test of the viability of natural-resources investing in Afghanistan. JPMorgan Chase assembled investors who ponied up $50 million for a mine in the rugged flyover country between Kabul and Herat.

JPMorgan bankers, drawing on knowledge of the country's natural resources from its mining clients in the former Soviet Union, shared some of that intelligence with Brinkley's team in 2008 and during the next two years worked to gather additional data. The results were presented to Petraeus and Defense Secretary Robert M. Gates last January. With the money raised, the mining project was granted a license late in 2010.

Ian Hannam, a managing director at JPMorgan who helped arrange the deal, says a successful mine has profound economic consequences. "With the mine comes a village, with the village comes a hospital and a school," he says. "Capitalism is like a good virus. You'll be amazed how quickly people turn up once someone has success."

Brinkley's charge is spreading that virus, and while he stresses realism, progress, and patience, he's hopeful. Back at Qala Ikhtyaruddin, Herat spreads out before him, its signature mosque jutting into the haze. The business tourists, having taken pictures all the way up, turn quiet.

Brinkley stands alone, resting his elbows on a massive ledge that looms hundreds of feet above a neighborhood of small homes. "I came here thinking there was nothing, but there's so much," he says. "This place, they really get it. All we need is time." Ⓑ

"With the mine comes a village, with the village comes a hospital and a school. Capitalism is like a good virus."

Ian Hannam, JPMorgan Chase

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Ten Years of ~~Inaccuracy and~~ Remarkable Detail: Wikipedia



How the online "temple of the mind" became the go-to site for looking stuff up: A drama told in the open-source style of Wikipedia. By Drake Bennett

This article was produced under a loose interpretation of Wikipedia's collaborative principles. Where indicated, it was rewritten, corrected, and commented upon by outside participants.

Guest Editors:

JONATHAN ZITTRAIN	ROBERT McHENRY	BENJAMIN MAKO HILL	MIKE SCHROEPFER
Professor of law and computer science at Harvard University	Editor-in-chief of Encyclopedia Britannica from 1992 to 1997	MIT researcher; Wikipedia editor; on Wikimedia Foundation advisory board	Developed Firefox open-source Web browser; now Facebook engineering VP

It's easy to forget, but 10 years ago it took serious effort to find decent information on the Internet. Searching the Web was like picking through a vast antique shop: There was the occasional find, and a lot of secondhand junk. Interested in Russian-made Tupolev airplanes? An obsessive hobbyist had a home page about them. Someone mentioned Volapük at a party? There was a university site with shards of information about the little-known language invented in the 19th century (not to be confused with the French avant-garde rock band of the same name). Then in 1999 came a simple idea from a search engine entrepreneur named Jimmy Wales: a free encyclopedia written by experts donating their time to draft articles and conduct peer review. The content would be copyable and ad-supported. It would be called Nupedia.

The site's team of PhDs moved at a pace that was indeed scholarly: In its first year, they created barely a dozen entries. Wales realized Nupedia needed a feeder site, something less exclusive that would attract writers. On this new site, any visitor would be able to write about whatever he wanted.

The experiment was unpopular with Nupedia's editors and advisory board—the fact that the uncredentialed were encouraged to contribute could, they reasoned, threaten the credibility of the encyclopedia. After less than a week, the new site was spun off into a separate project called Wikipedia—a "wiki" (Hawaiian for quick) is software that allows users to write, edit, and link Web pages on a single shared document. Within a year the new site had 20,000 articles. When Nupedia shut down in early 2003, it was stuck at 24 articles.



Tupolev Tu-334



German priest/Volapük creator Johann Martin Schleyer. Number of speakers today (estimate): 20.



ADDED BY ZITTRAIN, REPLACING:
"In early 2001, the creators of a nascent for-profit online encyclopedia called Nupedia grew frustrated with the slow pace of their project. In its first year, the site's team of volunteer PhDs had managed to create..."

Nupedia's first completed entry was on atonality



ADDED BY ZITTRAIN



Wikipedia co-founder Jimmy Wales



ADDED BY ZITTRAIN





A Wiki Wiki bus at Honolulu International Airport

WALES: GOH SENG CHONG/BLOOMBERG



MBS pioneered by Ginnie Mae in 1970



The Peace of Westphalia created the idea of nation-state sovereignty



ADDED BY ZITTRAIN



Pete Best

Jan. 15 is Wikipedia's 10th birthday. According to its own Wikipedia page, it has 17 million entries in more than 250 languages–including 118,000 in Volapük. The *Encyclopedia Britannica* has 120,000, and only in English. Free of charge–and of ads–the site is one of the most visited on the Web. It is the first stop for bar wagerers, high school paper writers, oppo researchers, and anyone trying to figure out what the Peace of Westphalia did or when the mortgage-backed security was invented or whom Ringo Starr replaced as the Beatles' drummer. The entry for the Deepwater Horizon oil spill went up on Apr. 21–less than a day after the rig explosion, and before anyone had any idea of its extent. "US Coast Guard has already launched a rescue operation," the article's last sentence read.





ZITTRAIN'S ADDITION DELETED BY HILL. COMMENT:
Removed sentence on Wikinews which seemed distracting and slightly off topic.

Even some of the site's staunchest supporters admit they initially doubted it would amount to much. The idea sounds like a utopian social experiment: a record of the world's knowledge, produced and policed by volunteers. Today anyone can still contribute to an entry, and many do. But rather than collapsing into chaos and endless arguments over the exact diameter of the second Death Star (a debate that, in fact, continues), the world of the self-proclaimed Wikipedians has grown into a thriving online society. "Its existence is proof of a radically different way of organizing production," says Yochai Benkler, a professor at Harvard Law School who studies social networks and the Internet.



Death Star diameter (estimate): 160 to 900 kilometers



ADDED BY ZITTRAIN:
"Indeed, the success of Wikipedia's own coverage of new events might help explain why Wikinews, a companion venture specifically designed to cover the news in a collaborative style, hasn't quite taken off."

Exactly what, though, does Wikipedia prove? The site has exponentially outgrown the humble expectations of Wales and co-founder Larry Sanger but has had to weather controversies over inaccuracy and manipulation. Recent years have brought complaints from contributors that the site is abandoning the welcoming ethos that once distinguished it, and voices inside and outside the Wikipedian community are questioning whether radical openness and accuracy can coexist. It remains to be seen whether Wikipedia's collaborative volunteerism can be applied to other realms, whether it can be preserved in Wikipedia itself, and–most fundamentally–whether it can produce something of reliable value for those not involved in the game.



ADDED BY McHENRY



Wikipedia co-founder Larry Sanger

Wikipedia was not the only online encyclopedia to be launched around the turn of the millennium. Along with Nupedia, there was an interlinked database called Everything2 where anyone could submit an article but no one could edit others' submissions. There was also H2G2, a playful miscellany inspired by Douglas Adams' *Hitchhiker's Guide to the Galaxy*. Before those there was Britannica, which had gone online quietly in December 1993. Microsoft's CD-ROM based Encarta, which was neither collaborative nor originally online, was



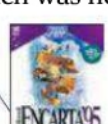
ADDED BY HILL



ADDED BY ZITTRAIN



ADDED BY McHENRY



Encarta, which Microsoft discontinued in 2009, had 62,000 entries



Fictional guide for interplanetary vagrants

TREATY: AKG-IMAGES/NEWSCOM; BEST: NEAL PRESTON/CORBIS; DEEPWATER HORIZON: U.S. COAST GUARD VIA GETTY IMAGES; FORECLOSURE SIGN: ARIEL SKELLEY/GETTY IMAGES

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Encyclopedia Britannica was first published in 1768



ADDED BY McHENRY



DELETED BY HILL: "programmer and" COMMENT: The fact that I'm a programmer isn't necessary I don't think.



DELETED BY HILL: "two" REPLACED WITH: "several key" COMMENT: My research shows more than two reasons.

seen as the primary digital threat to traditional encyclopedias like Britannica because it was given away free with new PCs.

According to Benjamin Mako Hill, a researcher at Massachusetts Institute of Technology who has looked at these early efforts, Wikipedia owes its success to several key decisions. "It's very tempting for people to say, 'We're online, now we're going to do something very different from what people did before,'" Hill says. But that would leave many contributors confused about what to contribute. Wikipedia didn't do that–the entries, though they're born of a new method of encyclopedia writing, are meant to read like the old *Britannica*.

Second, Wikipedia was user-friendly. Someone who found an error, or knew something about a subject that didn't have an entry, was a click or two away from taking action. The site's success attracted still more contributors. Soon scholars like Benkler and Clay Shirky were celebrating Wikipedia as a prime example of how the Web could upend assumptions about human motivation and organization. Here were people contributing hours of their time, gratis, to build what Wales called "a temple of the mind." Wikipedia's model bears much similarity to free and open-source software that took off in the 1990s with the release of Linux and Mozilla. But Wikipedia, with its diverse, international body of contributors, couldn't just be dismissed as a cultural oddity or a particular slice of geekdom–at least not after it expanded beyond physics equations and *Star Trek* recaps and into the rest of humanity's hard-won knowledge.

Still, concerns about the site's accuracy grew along with its influence. As the satirical newspaper *The Onion* put it in a recent headline: "Wikipedia Celebrates 750 Years Of American Independence." In most widely read entries, falsehoods are quickly corrected, but in others misinformation can survive far longer. In the fall of 2005, John Seigenthaler, a former aide to Robert F. Kennedy and the founding editorial director of *USA Today*, discovered that a Wikipedia page named him as a suspect in RFK's assassination. More than four months after the false charge was published, the entry was finally corrected. Seigenthaler did not correct the entry himself; he wrote an op-ed for *USA Today* pointing out Wikipedia's inaccuracies. The incident led Wales to acknowledge that entries were being written faster than they could be reviewed, and to announce a policy where unregistered users would no longer be able to create entries. (Registration is free and instant, and does not require personal information.)

One of Wikipedia's loudest critics is co-founder Sanger, whom Wales laid off when the dot-com bubble burst. For Sanger, scandals like the Seigenthaler episode can't be avoided without changing Wikipedia beyond recognition. "I just don't think it's really even possible given the nature of the project," he says.



ADDED BY SCHROEPFER



The *Star Trek* entry has been revised 9,701 times



Clay Shirky, Internet pundit



ADDED BY ZITTRAIN



ADDED BY ZITTRAIN



ADDED BY McHENRY



ADDED BY ZITTRAIN

2007 headline: "Hard To Tell If Wikipedia Entry On Dada Has Been Vandalized Or Not"



John Seigenthaler



Robert F. Kennedy

BRITANNICA: PRNEWSFOTO/ENCYCLOPAEDIA BRITANNICA, INC./AP PHOTO; SHIRKY: ZUMA PRESS/NEWSCOM; KENNEDY: ED CLARK/TIME LIFE PICTURES/GETTY IMAGES; SEIGENTHALER: MARK HUMPHREY/AP PHOTO; ENTERPRISE: PARAMOUNT PICTURES/EVERETT COLLECTION




Marty Meehan, now chancellor of the University of Massachusetts-Lowell


ADDED BY ZITTRAIN

In 2006 Sanger started Citizendium, a competing wiki-based encyclopedia with "gentle expert oversight" and contributors who use their real names.


DELETED BY ZITTRAIN: "... one-third more errors..."


SCHROEPFER COMMENT ON McHENRY EDIT: Agreed–that's a pretty significant difference.


ADDED BY McHENRY


ADDED BY ZITTRAIN

At the same time, analyses of Wikipedia's accuracy have generally found that, while it's occasionally wrong, it's not much more wrong than traditional encyclopedias. A 2005 study in the journal *Nature* found that in a sample of articles, there were an average of 2.92 mistakes per article for Britannica and 3.86 for Wikipedia. (Britannica objected to the *Nature* study, calling the methodology "fatally flawed.") Wikipedia, however, has problems Brittanica doesn't. An error corrected in Britannica stays corrected; in Wikipedia, it may not. (By the same token, rapidly changing events can be covered in pace by Wikipedia.) Then there are the tastes of its editors. Popular culture looms large. The entry for the video game Halo, for example, is significantly longer than the one for the Protestant Reformation.


ADDED BY McHENRY


DELETED BY McHENRY: "...Wikipedia was only slighly less accurate than Britannica."
REPLACED WITH: "...Wikipedia had one-third more errors than Britannica."
COMMENT: One-third more is not "slightly more" in my book.

More seriously, Wikipedia has to weed out inaccuracies introduced not by accident or through the ignorance of contributors but intentionally. Sometimes, as in the Seigenthaler case, these are instances of vandalism. Other times it's résumé-polishing. In 2006 aides for Massachusetts representative Marty Meehan removed a Wikipedia mention of his campaign promise not to serve more than four terms–at the time he was on his seventh. Wales has edited his own bio page, deleting mentions of Sanger's role in the creation of Wikipedia.

60

Thanks to WikiScanner, software that cross-references the Net addresses of contributors, watchdogs have found that computers at ExxonMobil, PepsiCo, and Diebold, among others, have been used to remove unflattering information from the companies' entries. Last year, Wikipedia's arbitration council banned edits from all IP addresses owned by the Church of Scientology after years of dispute and deceptive editing by both adherents and critics of the religion.

Many of these worries apply to businesses that have taken parts of Wikipedia's model and monetized it. TripAdvisor and Yelp have created democracies of taste, empowering travelers and consumers to speak up and create a far greater wealth of opinion than any team of professional reviewers could. Still, the owners of the reviewed hotels and restaurants complain that the sites' anonymity allows for slander without repercussion.

Wikipedia has experimented with concentrating more power in the hands of "administrators," a select group of Wikipedia editors who have the ability to delete and restore oft-manipulated pages and to lock them down for a period of time to prevent further edits. These changes have brought a measure of stability to certain entries. (George W. Bush's is getting vandalized less often. During his Presidency, his picture was swapped with one of Hitler; he was described,


Length of Wikipedia entry for Halo: 9,000 words. Protestant Reformation: 7,800 words.


PepsiCo: "It's really a simple matter of ensuring that our Wikipedia entry provides an accurate description of our company"

DIEBOLD

Diebold: "It was somebody within our building but it wasn't an official corporate communication effort"

Church of Scientology: "We hope it results in more accurate and useful articles on Wikipedia"



ExxonMobil: "Employees are not authorized to update Wikipedia with company computers without corporate endorsement"

MEEHAN: JAMIE ROSE/GETTY IMAGES; EXXON: KAREN BLEIER/AFP/GETTY IMAGES

parc
Palo Alto Research Center

Birthplace of the graphical user interface



Peak number of active editors: 820,000 in 2007



ADDED BY McHENRY

briefly, as "the first person ever to masterbate [sic] in a public school more than 38 times.") But Wikipedia discussion boards are full of complaints about entries getting locked down without proper cause. And there seems to be no mechanism for assuring that administrators are knowledgeable about anything beyond the methods and rules of Wikipedia itself.



COMMENT:
Two separate issues here.
A) Anonymous contributions - people generally act more civilly if their reputation is on the line.
B) Control by a trusted set of admins. This model has been successfully used in Open Source Software projects where trusted gatekeepers monitor and approve the contributions from a much larger set of contributors.

The worry for some who have followed the encyclopedia over its first decade is that as the site matures, it will have a harder time attracting and retaining the volunteers who make it work. A research team led by the computer scientist Ed H. Chi at Xerox PARC has found that Wikipedia's growth, whether measured in entries, edits, volunteers, or even bytes, has been falling off for a few years. The number of active editors and rate of article creation both peaked in 2007. The site, Chi argues, has begun to behave less like a limitless information ecosystem and more like a biological one, a world where actors compete over limited resources. Today, all the obvious entries–Aristotle, electricity, the Magna Carta, the American Civil War–have been written, along with millions more. That leaves fewer new ones to write and increases the chance that a new entry will be deleted on the grounds that it, as Wikipedia's guidelines say, "lacks notability." An entry written by Wales himself about a South African restaurant was deleted on the grounds that it contained "no assertion of importance/significance." (It has since been reinstated.) But the main effect of the new competitiveness is to drive out newcomers, whom Chi found are more likely to have their entries and edits rejected.



American Civil War: First Wikipedia entry, published Nov. 2, 2001



COMMENT:
The open source analogy fails, though, at two points: The one where the developmental software is identified as such, and the one where the product is tested against some objective criterion. The software runs or it doesn't; the article, good or not, simply gets published to the world.



"Mzoli's Meats is a butcher shop and restuarant located in Guguletu township near Cape Town, South Africa" —Jimmy Wales, Wikipedia, Sept. 17, 2007

Andrew Lih, a Wikipedia administrator and the author of *The Wikipedia Revolution*, says there was a feeling of euphoria when he joined the site in 2002. "There were only 30,000 or 40,000 entries," he says. "You'd look up Angkor Wat, and there'd be only one line. You'd add a paragraph or two. Someone else would come along and say, 'That's cool, here's some other stuff.' You'd look at a site on the Egyptian pyramids and borrow from it. It was empowering." Today, he says, the feeling of the place couldn't be more different. Wikipedia's overwhelming popularity has brought new scrutiny, and these days, Lih says, the dominant concern is protecting what's already there. "The environment today is, like, 'Don't touch anything,'" Lih says.

The problem, as Lih sees it, is that Wikipedia actually needs more eyes than ever. As PR firms, image consultants, and congressional aides get better at subtly shading entries, it's going to take more and more volunteers to shade them back. Even the most seasoned administrator was once, in Wikipedian argot, a "clueless newbie." How well Wikipedia ages may depend on how much the newbies are allowed to grow up, too. B



COMMENT:
If the number of articles is growing less quickly - then I don't agree that more volunteers are needed. Also there is an assumption here of the unbiased nature of existing volunteers and the biased nature of new ones.



Aristotle, father of formal logic

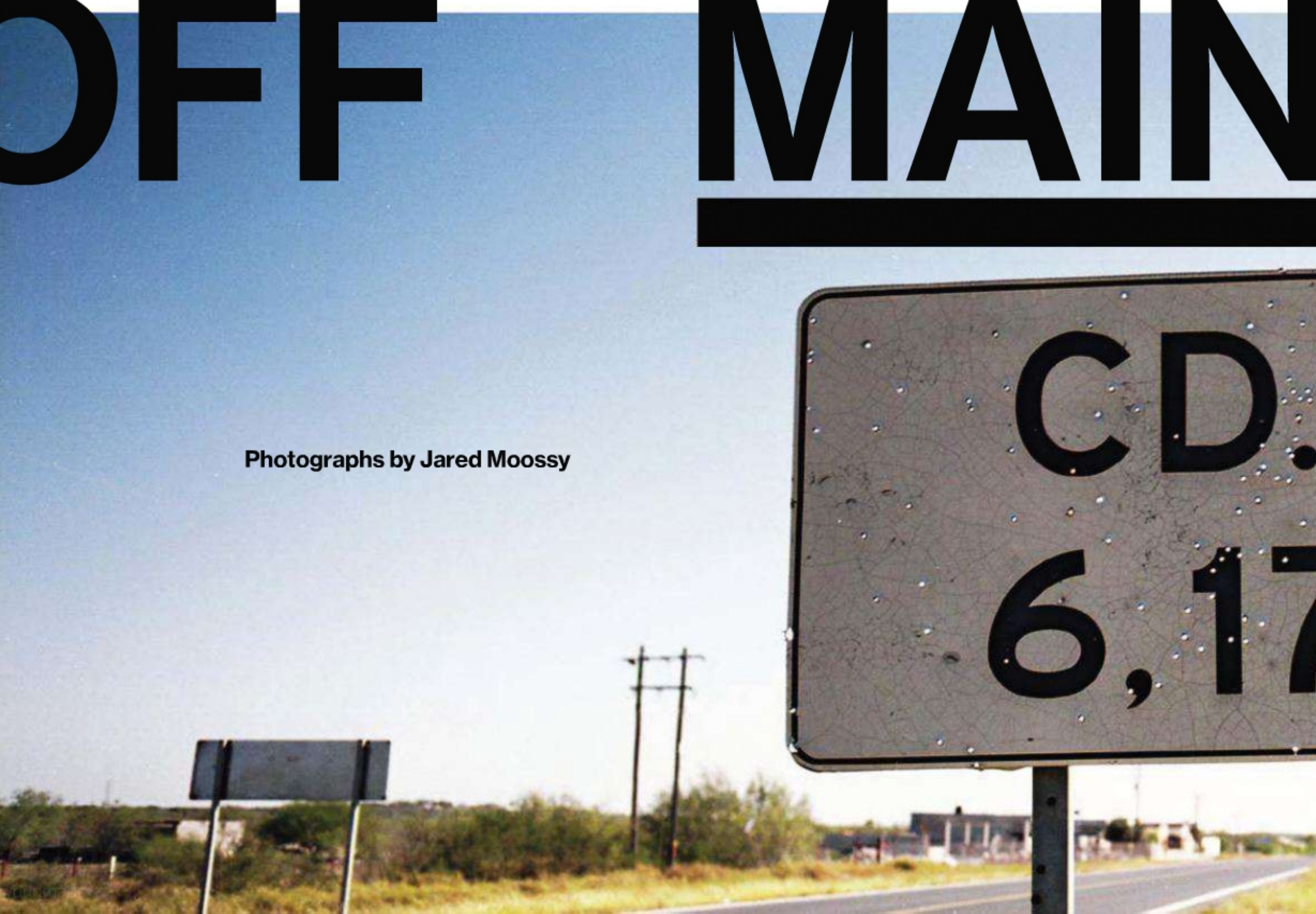


According to Wikipedia, "the world's largest religious building"

LAPTOP: SYLVAIN SONNET/GETTY IMAGES; ANGKOR WAT: ANGELO CAVALLI/AGE FOTOSTOCK AMERICA; ARISTOTLE: DEA PICTURE LIBRARY/GETTY IMAGES; STEAK: STEVE WISBAUER, GETTY IMAGES; CANNON: BRAND X PICTURES/GETTY IMAGES

worldmags

WHEN UNDERG
KILLS
OFF MAIN



Photographs by Jared Moossy

THE GROUND ECONOMY

The Mexican border town of Ciudad Mier emptied in mid-November. More than 6,000 inhabitants fled as rival drug gangs shot up the place with bazookas, rocket-propelled grenades, and rifles, threatening to kill anyone who dared stay. And so the drug trade, the most virulent of black markets, claimed another victim: an entire town.

STREET



worldmags



As the drug gangs—the Zetas and the Gulf Cartel—escalated their war in Ciudad Mier, on the Texas border 250 miles south of San Antonio, residents took shelter in the nearby town of Miguel Alemán. The town's Lions Club, pictured here, reportedly became Mexico's first haven for victims displaced by drug violence, housing more than 300 refugees. Today, less than 20 percent of Mier's population is back, says Maria Silvia Ramos, a town hall spokeswoman, and some 20 percent of businesses have reopened.



Cartel attacks on law enforcement officials have been particularly gruesome. During a firefight that lasted for several hours on Nov. 15, warring gangs pillaged Mier's police station and chased the officers out of town. The police have yet to return. Above, military patrols photographed through the station's shattered windows. Below, the station's charred interior.



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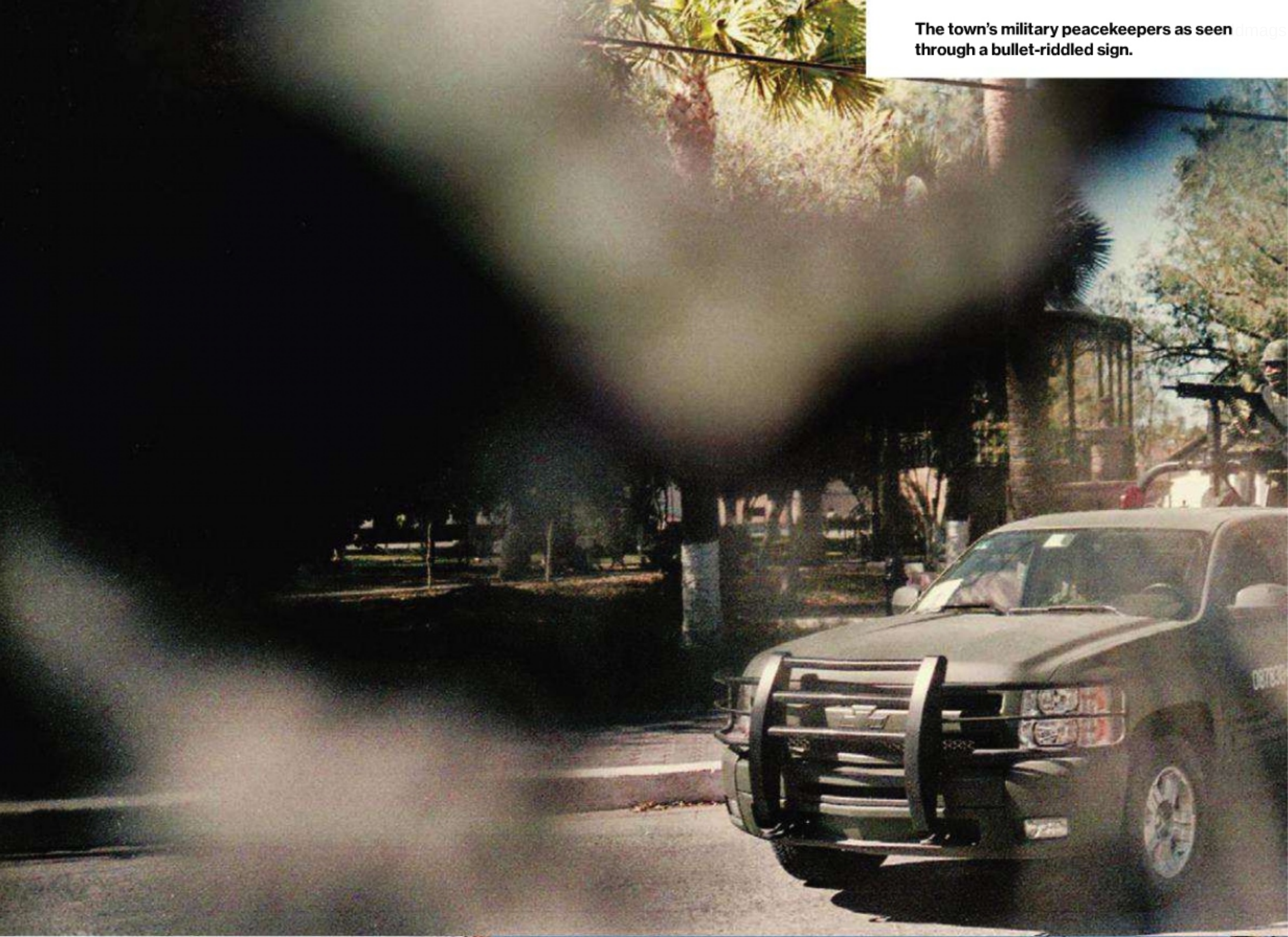


A bullet-riddled file cabinet in Mier's police station. Mexico's drug-war death toll has climbed to more than 30,000 since President Felipe Calderón took office in December 2006, according to Mexican Attorney General Arturo Chávez. Of those, more than 12,000 took place in 2010.

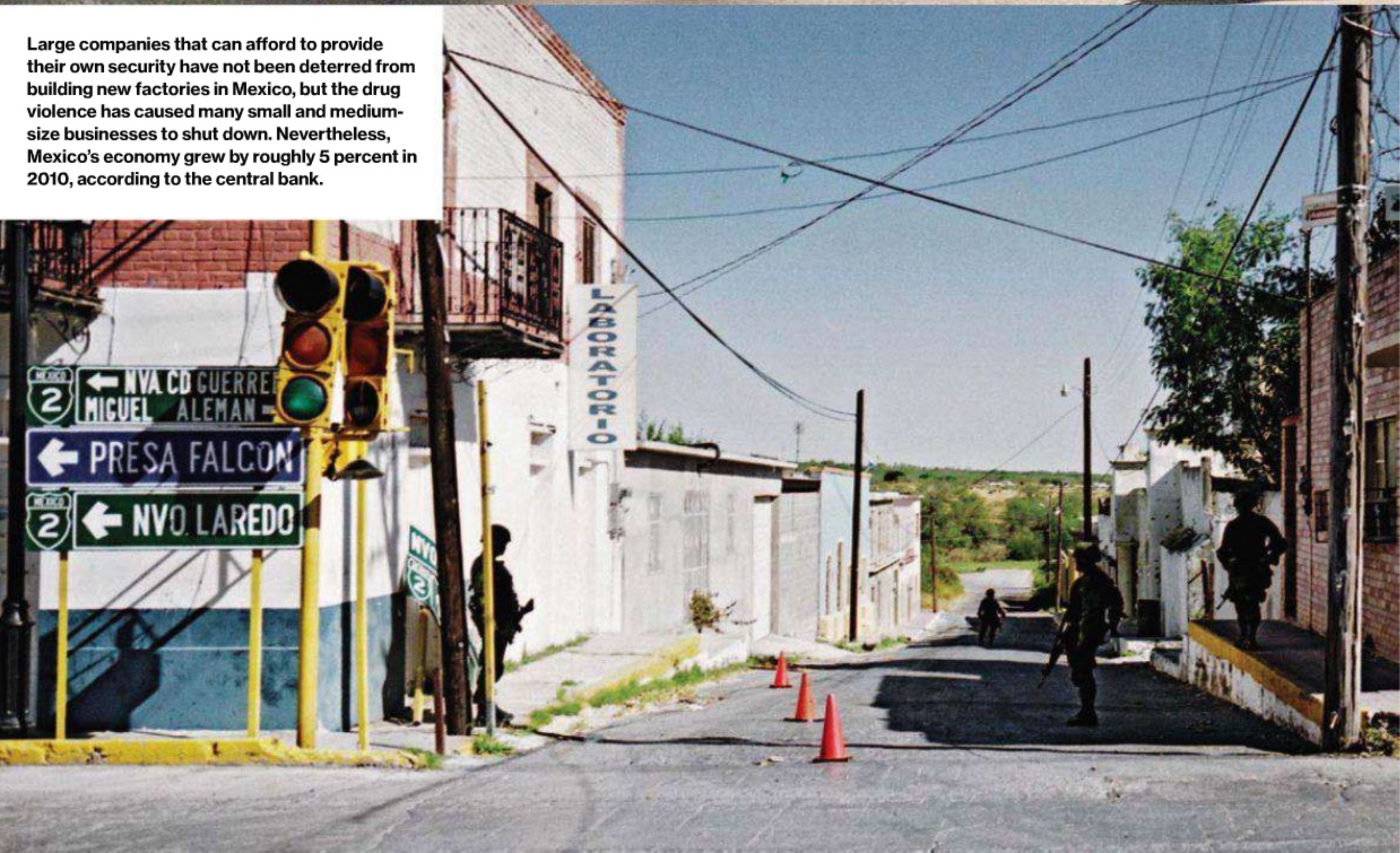


Remaining residents attend Mass in Mier's main cathedral. During the ceremony, they pray for peace and sing an *anti-narcocorrido*—an anti-drug-gang song intended to counter the popular *narcocorrido* genre, which glorifies smuggling, murder, and extortion.

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The town's military peacekeepers as seen through a bullet-riddled sign.



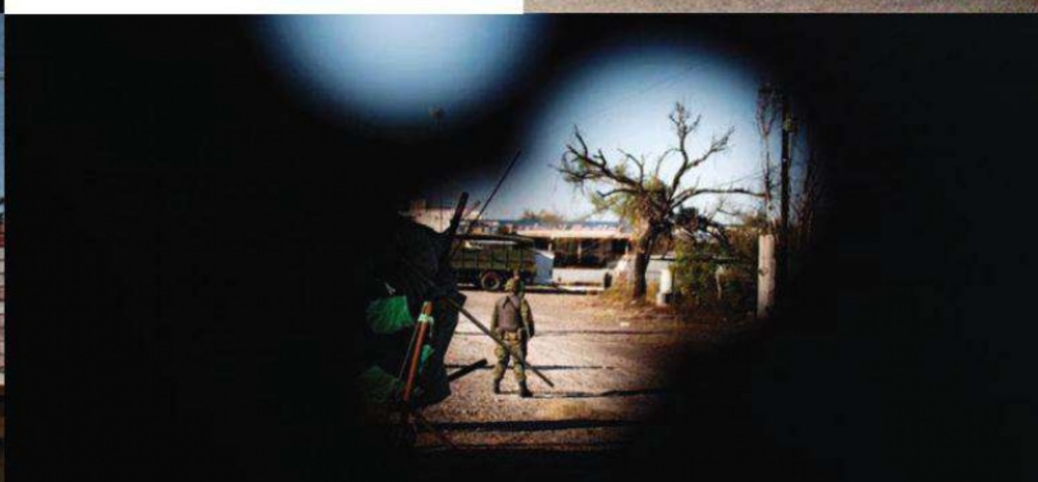
Large companies that can afford to provide their own security have not been deterred from building new factories in Mexico, but the drug violence has caused many small and medium-size businesses to shut down. Nevertheless, Mexico's economy grew by roughly 5 percent in 2010, according to the central bank.

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Over the past 10 months cartels attacked Mier's infrastructure, at times cutting off the water and power supplies. Below, soldiers patrol the desolate town. Fighting continues along Mexico's northern border, where cartels vie for control of smuggling routes to the U.S. Mier's empty streets, once known for their colonial grace, are evidence of a growing exodus from the region.







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Foreign Language Software



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A former hedge-hog sells bivalves
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The Mark Zuckerberg of Asian street-wear couture
Page 74





Matchmaker, Catch Me a Czech

Or a Russian. Or a Ukrainian. The shaky global economy is helping the international mail-order-bride trade flourish. *By Teddy Wayne*

Photograph by Anthony Redpath

worldmags

Etc. Mail-Order Brides

Times are good for Joseph Weiner. The former investment banker and Wharton MBA lives with his wife of 27 years in a three-bedroom London townhouse. When he isn't lounging in his private garden, Weiner spends his free time playing tennis at the exclusive Hurlingham Club and gliding around town in his Lexus. Though he doesn't claim to be a philosopher, Weiner's insight into the human heart has led to a lucrative second career as a matchmaker and packager of amorous adventures. "Every guy wants a beautiful younger woman," he explains. "It's the nature of us."

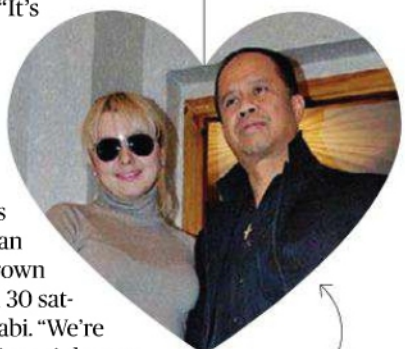
Fourteen years ago, Weiner, 73, founded Hand-In-Hand, a London-based matchmaking agency that charges male customers up to $2,000 for a "supervised courtship"—a process that matches them with younger Eastern European women. Hand-In-Hand has since grown into a multinational operation with 30 satellite offices from the U.S. to Abu Dhabi. "We're still opening up franchises, and business is booming," says Weiner in his thick New York accent. "Financial problems are the biggest cause of divorce. There are more financial problems now. There are more people available!"

In the age of globalization, the international matchmaking industry—still known in many circles as the mail-order bride trade—is thriving like never before. The Tahirih Justice Center, a nonprofit organization in Falls Church, Va., that protects immigrant women, estimates that the number of mail-order marriages in the U.S. more than doubled between 1999 and 2007, when up to 16,500 such unions were sealed.

International matchmakers are now a growing segment of the U.S. online dating industry, which, according to market research firm IBISWorld, racked up more than $2 billion in 2010 revenue. Since the recession began, "we've seen more men sign up," says John Adams, the co-founder of Phoenix-based A Foreign Affair, which charges $4,000 for the right to attend champagne-soaked "socials" in various Eastern European cities. The company estimates it sparked nearly 1,000 engagements this year. "Men evaluate their lives a little more closely when the economy becomes more difficult. They look at what's really important to them and try to find that one person they want to spend the rest of their lives with." Adams would know. He met his wife, Tanya, at a 1997 St. Petersburg social sponsored by his own company.

Amid the proliferation of dating websites and matchmaking reality shows, venturing abroad for love has taken on a more acceptable mien. International matchmakers have succeeded, in part, by targeting middle-aged men who find dating troublesome—men who, according to Weiner, "don't have the money to go out on dates and go on weekends to Vegas and Atlantic City. They want someone to take care of them." While they might not have the means to secure a more conveniently located trophy wife, they must have enough money to travel to Eastern Europe and spend thousands for a shot at eternal bliss. Though love may be priceless, notes Weiner, "$2,000 to get a beautiful woman—it's a bargain!" According to David L. Knabel, the owner and president of Louisville-based matchmaker A Volga Girl, "It's no different than a dating site in the U.S.—except it's international marriage."

"It's no different than a dating site," says the owner of A Volga Girl



Insurance salesman Ben Baligad and his potential bride, Natalya Chuprina

In 2007, Ben Baligad hit a dry spell. The divorced 53-year-old eschewed the San Diego dating scene after discovering Ukraine's favorable gender ratio—0.92 males for every female between ages 15 and 64, according to the State Statistics Committee of Ukraine. After enlisting companies such as Global Ladies and Army of Brides, the insurance salesman made three trips to Ukraine. The third time was the charm: Baligad met his potential future wife, Natalya Chuprina, 18 years his junior. "I'm planning on bringing her to the U.S. as soon as I get my finances straight," he says.

By pulling on the heartstrings of single men, the mail-order bride industry has at its disposal untold financial opportunities. In addition to membership fees—which run $29.95 per month at A Foreign Affair—and "romance tours" that can cost suitors thousands, many sites charge between $6 and $8 to translate each e-mail exchanged between interlocutors, and even more for phone and instant message translation. Some companies, like Hand-In-Hand, have also expanded into same-sex international matchmaking. "We've been doing gay business for about a year and a half," boasts Weiner.

Though every site claims to police its users, scams are

How to Meet, and Perhaps Marry, Your Own Mail-Order Bride

Lonely, culturally adventurous, or too busy to date? Follow this primer to your heart's content.

Step 1 *check here* ☑



Find a site that directly connects you to verified female members. Giveaways that the site is iffy include exorbitant fees for translation, phone interpreters, and options such as: "check box to accept minimum credit-card charge to date with beautiful woman from Ukraine."

Step 2 ☐

Voluntarily disclose any criminal records through the International Marriage Broker Regulation Act. It's on the honor system, which is a perfectly sensible method for weeding out former criminals.

Step 3 ☐



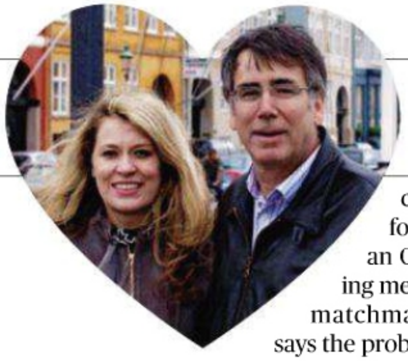
Bypass the galleries filled with flaxen-haired, buxom 22-year-old fitness models and ungrammatical come-ons.

Step 4 ☐



Instead, contact 54-year-old Irkutsk schoolteacher Olga. She's real—and probably more than eager to get the hell out of Siberia.

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A Foreign Affair co-founder John Adams met his wife, Tanya, at a "social"

common. Les Vancil, the founder of Easy Ukraine, an Ohio-based site targeting men traveling abroad for matchmaking opportunities, says the problems lie with the Eastern European agencies contracted to recruit women. Vancil asserts these companies post fake profiles, ratchet up prices for translation, and sometimes impersonate women to ask for money.

When customers complain, matchmakers "wipe their hands clean," says Steve Ewald, a Detroit accountant who stopped using such sites after several unsatisfying experiences. They blame the agencies, he claims, who blame the women. Ben Baligad says the agency that helped him communicate with his girlfriend skimmed 10 percent off the money he sent her for train fare and phone bills. He also suspects it posed as her in e-mails demanding he pay for a pricey apartment rental for his visit. He hasn't brought it up with his girlfriend, though. "I think she thinks I will get angry," he says.

The arrangement can be far worse for the women involved. After a few highly publicized murders of women brought to America through international matchmakers, the U.S. passed the International Marriage Broker Regulation Act of 2005 (IMBRA). The statute requires background checks on U.S. citizens before communication via the matchmakers. Those who fail to comply cannot obtain a Form I-129F, Petition for Alien Fiancé(e).

However, couples can get around this obstacle by claiming they met through other avenues. There also tends to be little enforcement of IMBRA when the agencies are based outside the U.S. (Hand-In-Hand, for example, is registered in St. Kitts.) "The mail-order bride industry is a softer version of human trafficking," says Sonia Ossorio, executive director of the New York City chapter of the National Organization for Women. Ossorio also acknowledges that some relationships work out—but perhaps not in a way that would please Betty Friedan. "A lot of people who are attracted to it are just looking for a woman who's docile and obedient," she says.

"The mail-order bride industry is a softer version of human trafficking"

For some companies, such submissiveness is a selling point. Hand-In-Hand's website trumpets the fact that its females are "unspoiled by feminism." Company founder Weiner argues this form of chauvinism—like the mail-order bride business itself—is economically motivated. "You take a beautiful woman from the Czech Republic and you bring her into your home, she does all your cooking and cleaning and ironing," he says. "At the end of the day, the service is free." Hand-In-Hand estimates the potential savings of a homemaking wife at $150 per week.

Women from economically troubled regions also take part in order to secure an American visa. "People around the world still view the U.S. as a highly favorable place to live," says A Foreign Affair's Adams. His wife agrees. "I worked a lot before, but then I was waking up at nine in the morning and was like, 'Whoa, what do I have to do now?'" says Tanya Adams, who remains a supporter of the company. "I even recommended it to my niece."

Perhaps love can always find a way. Most sites claim a 75 percent or greater success rate, and this boundless quest for passion—one inflamed by hard times—continues to benefit matchmaking entrepreneurs. "Wonderful times for me," Weiner says. "I can't complain." Ⓑ

ILLUSTRATIONS BY BROWN BIRD DESIGN

Step 5 ☐

After you've established contact with a woman, be prudent about sending money if she requests it. While it may be true that there's no romance without finance, be wary when a potential spouse asks you to pay for hotel rooms for her entire family—and a $1,500 "house-call license."

Step 6 ☐



Take a trip to meet the woman in her native country, but be wary of suspicious economic arrangements she may have initiated, such as inordinately high fees for her transportation or a pricey hotel she has lined up.

Step 7 ☐



If you have not connected with a woman on your own, sign up for a "romance tour" providing a few "socials" with hundreds of women in a nightclub atmosphere filled with booze.

Step 8 ☐

Propose against a romantic backdrop of cement-block housing units constructed for maximum utilitarian value.

Step 9 ☐

File Form I-129F, Petition for Alien Fiancé(e) ($340) with the U.S. Citizenship and Immigration Services office. After it's processed (the average wait: one to three months), your fiancée can file through her country's U.S. Embassy or consulate for a K-1 nonimmigrant visa ($350), which permits her to travel to the U.S. and marry you within 90 days, pending approval of a visa interview (waiting time: a few days to many months), supporting documents (possibly including form I-134, Affidavit of Support, attesting to financial sponsorship; $88 if reviewed in the U.S.), evidence of a relationship, and a medical exam. Revel in the whimsical spontaneity of love.

Step 10 ☐



Bring your betrothed back to America. After spending thousands of dollars on meeting her and immigration fees, tell your friends you met at the supermarket.

Gaming in the Cloud

OnLive's on-demand service may make costly hardware boxes obsolete. *By Rich Jaroslovsky*

Imagine playing video games on an Xbox 360 or PlayStation 3 attached to your TV, a stack of disks nearby. Now take away the Xbox and the disks, and you'll get the idea behind OnLive. Using a palm-size MicroConsole adapter hooked up to your TV and home network, you play "in the cloud"—over the Internet, with the games actually running on powerful servers that might be 1,000 miles away.

This has the potential to be disruptive, maybe even revolutionary, technology. The $99 adapter plugs into a high-definition port on your television, and comes with a wireless handheld controller and one game. The system doesn't work over Wi-Fi, so a hardwired Internet connection is required. This isn't a problem if your TV is located near your router; if it isn't, you'll have to come up with a solution, such as using adapters that transmit a signal over your electrical wiring.

Most of the 50 or so available games are cheaper to buy than on Xbox and PlayStation, and OnLive is also introducing a Netflix-like all-you-can-play plan for $9.99 a month for a selection of its titles. While you won't find many newly released games—and a couple of major publishers are missing—you'll still come across some recent, recognizable hits.

Hard-core gamers debate whether OnLive's response times are fast enough and whether graphics look as good as they do on a dedicated console. As long as you have a solid network connection, play moves swiftly, and video is stutter-free. While graphics quality varies among titles, the differences between the OnLive and console versions are all but invisible to the untrained eye.

Because OnLive is a service and not just hardware, it offers some cool additional features. You can play on a computer as well as on your TV, starting a game on one device and picking up where you left off on the other. You can create and share a "brag clip," while a mode called Arena lets you watch someone else's game in real time and register digital cheers or jeers at their performance.

Like Netflix, OnLive may eventually be built into other devices; it announced a deal with TV manufacturer Vizio at last week's Consumer Electronics Show. OnLive has answered the biggest question about itself: It's for real. But it still needs to beef up its library—and get that Wi-Fi issue taken care of—before it's really cloud nine for gamers. B



THE POPULARITY GAME

Four of OnLive's top offerings



Assassin's Creed II

Roam around the deadly, assassin-plagued world of Renaissance-era Italia.



Batman: Arkham Asylum

Take on Gotham's greatest villains using Batman's arsenal of tricks and gadgets in this 2009 cult favorite.



NBA 2K11

Play against classic NBA teams of the past, such as Michael Jordan's late-1990s Bulls, in this 2010 hoops challenge.

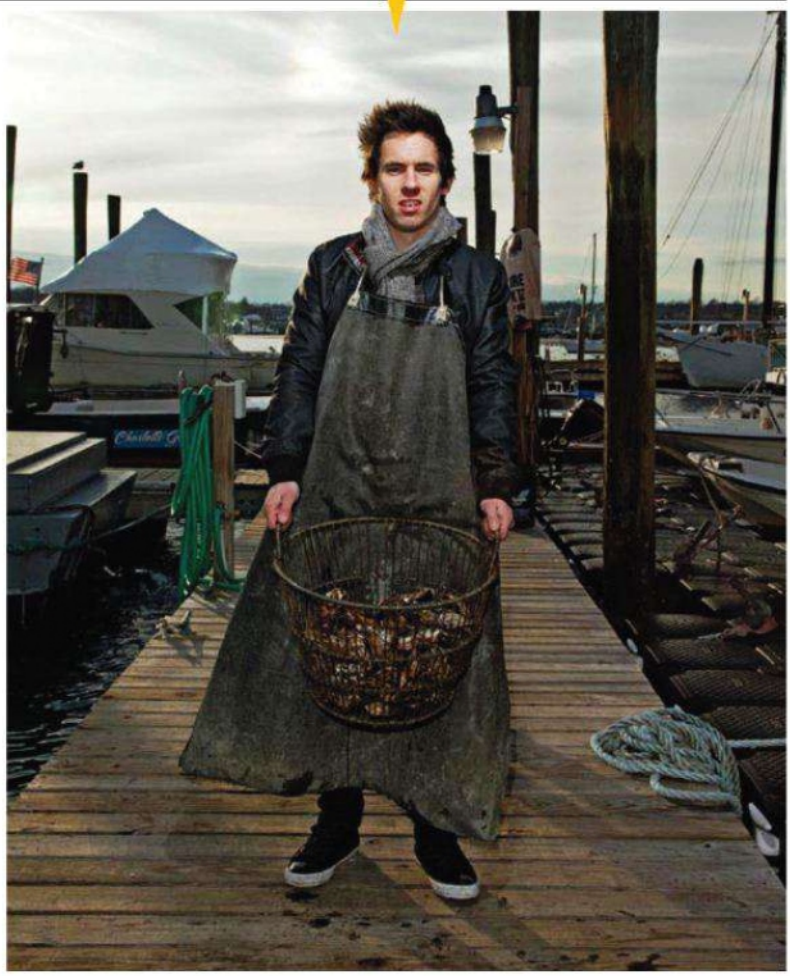


Shaun White Skateboarding

While skateboarding on city plazas and buildings, try more than 80 tricks picked by superstar Shaun White.

The Waterboy

After leaving finance, Northrop started oyster farming in Westport, Conn.



Jeff Northrop left the hedge fund world to begin shucking around town. *By Alexandra Wolfe*

When he left the New York offices of Exis Capital Management, Jeff Northrop thought he was leaving behind the expense-account restaurants where his fellow financiers held court. He regained entry into those gilded boîtes through the kitchen door. These days, Northrop makes his living by selling them oysters.

Born in Westport, Conn., Northrop, 25, was raised on the water. His father was a fly-fishing guide who also sold watercraft. Instead of aspiring to work in the family business, Northrop armed himself with an economics degree from Columbia University, and in 2009 took a job as an analyst at Exis. He quickly became disillusioned monitoring the portfolio manager's list of stocks and futures. And then there was the work environment. "The office had like 15 different climate zones," remembers Northrop. "Depending on [his boss's] stress level, he would want it warmer or colder." He left within six months.

Around this time, Northrop's father discovered his family owned a sizeable acreage of oyster beds near their Westport property. His father had been selling molluscs to local restaurants, but Northrop suggested expanding the business by offering oysters to posh Manhattan restaurants. With $100,000 of his and his father's savings–plus $35,000 from a former Exis colleague–Northrop incorporated Westport Aquaculture (now called New York Oyster Co.) in July 2010.

An early break came when a friend introduced him to the owner of Lavo, a recently opened Midtown playpen for aspiring jet-setters. Northrop soon began approaching other potential customers cold. Barry Frish, sous-chef at Tribeca's Marc Forgione, remembers Northrop's boldness. "Walking through the door with a box of oysters on ice was definitely a selling point," he says. Now the company supplies 35 restaurants, including Manhattan stalwarts such as Daniel and Balthazar.

While Northrop says his company will sell $450,000 worth of oysters this year, he's not satisfied. His longer-term objective–a marriage of his past and present careers–is to raise money to invest in sustainable fish farms. "My end goal," he says, "is to create the world's first aquaculture hedge fund." (B)

Northrop's oysters are 55¢ to $1 each, wholesale



STREAM OF REVENUE

12
Hours it takes Northrop to deliver oysters from harvest to chef

100+
Number of hours per week he worked in finance; the same as in oyster farming

$3-$3.75
Average final price of the oysters, including markup, at Manhattan restaurants

15,000
Oysters delivered to dining spots in New York City on New Year's Eve

DATA: NEW YORK OYSTER CO.

FROM TOP: PHOTOGRAPH BY ANDREW HETHERINGTON FOR BLOOMBERG BUSINESSWEEK; ISABELLE ROZENBAUM AND FREDERIC CIROU/GETTY IMAGES


Urban couture designer Koon ponders world denim domination at his Manhattan studio

The Fresh Prince Of Streetwear

Jonathan Koon, auto-pimping mogul and designer, wants to be a billionaire by 30. *By Joe Pompeo*

Wearing red Hermès sneakers, a gray smoking jacket-cardigan hybrid of his own design, and five pounds of pure gold draped around his neck, Jonathan Koon walks around his Midtown Manhattan showroom inspecting his new line of high-end denim. Nearly a dozen pairs of hand-washed, uniquely distressed and abraded jeans from his spring 2011 collection are laid out on a coffee table. Koon picks up one pair and turns a pocket inside out to reveal his signature sartorial touch–an ancient Chinese poem, "Bringing in the Wine," by the scholar Li Bai, inscribed in the fabric. "It basically says, 'If there's a chance to be happy, or a chance to drink, drink and be happy to your heart's desire,'" Koon translates.

Koon's line of Asian streetwear couture was launched on Jan. 3

It also describes Koon's philosophy. The precocious auto accessories mogul and ghetto-fabulous branding guru wants to be the Mark Zuckerberg of Asian streetwear couture. With the Jan. 3 launch of his Private Stock clothing line, Koon, 27, is hoping Americans will go as gaga for his Hong Kong-inspired jeans as they once did for Italy's Diesel brand. Maurizio Marchiori, Diesel's former U.S. marketing chief, is already a believer. "Jon has great potential," says Marchiori, who mentored Koon through the design process. "This guy's not a designer, he's a visionary."

While Koon may dress like a rapper and talk like a quant, he's already thinking like a mogul. "We'll be the next big denim company," he says. "A billion-dollar company." The first generation Chinese American has invested $2 million of his own money in Private Stock, which he's soft-launching with 11 denim styles (priced between $110 and $325) and roughly

the same number of polos and button downs along with lightweight jackets, bracelets, and watches—all befitting a modern adaptation of *West Side Story* set in the streets of Hong Kong. Certain limited-edition styles will be sold for up to $1,195 per pair.

Unlike many aspiring fashion designers, Koon is already a multimillionaire, having made a fortune tricking out cars. While attending Manhattan's prestigious Stuyvesant High School, he and a friend launched Extreme Performance Motorsports with $10,000 of their personal savings. They opened wholesale accounts with Asian auto distributors and started importing custom body kits, aftermarket wheels and rims, floormats, stereo systems, and all manner of specialized accessories that—in the age before MTV's *Pimp My Ride*—helped usher in the blinged-out car craze. "It was almost like a virus that spread," says Koon. "We struck a fair amount of success very quickly." Koon says he made a million dollars within a year.

After shuttering the business while attending Georgetown University, Koon struck gold again, in 2004, by patenting Dubz, a hugely successful air freshener designed like a spinning car rim. He subsequently launched Sparkz (a lighting accessory), Klipz (a cell phone holder), and Ionik (an air ionizer), which helped establish his brand among record label executives and rappers. In 2008 hip-hop star Young Jeezy made Koon the exclusive partner in his apparel line, 8732. The clothing company now falls under the umbrella of Tykoon Brand Holdings, which is based in his native Queens, N.Y. The 27-person, privately held company, Koon claims, is worth $80 million.

Soon after joining 8732, Koon's obsession with car parts was replaced by a fixation on street fashion. He traveled through Europe and Asia to scrutinize local styles and learned how to distress jeans at a denim washing house in Japan. Koon's curiosity soon led him to start creating one-off trousers for what he describes as "big-time pop stars in Hong Kong and Tokyo," though he declines to divulge their identities—"I don't wanna name-drop," he demurs.

Koon also caught the attention of Italian luxury goods designer Domenico Vacca. The two teamed up to create the Domenico Vacca Denim Collection, which landed in the designer's boutiques last May and now falls under the Tykoon umbrella. "It looks like an unlikely partnership, but each is bringing something to the table," says David Lipke, who covers menswear and denim for *Women's Wear Daily*. "Domenico Vacca has a base of loyal clients that like his approach to somewhat fashion-forward gentleman's tailoring, and Jon Koon brings a youthful attitude and some expertise in sportswear manufacturing."

Breaking into the premium denim market on his own, though, will be a tougher challenge. It's a highly competitive field, says Lipke, since it's an

"This guy's not a designer, he's a visionary"

attractive starting point for upstart designers and entrepreneurs. "There are a multitude of brands in the denim category, and the ones that thrive have dedicated, astute people behind them who live and breathe denim," he says. Newer companies such as Hudson, J Brand, and AG Adriano Goldschmied were built from scratch and have come to saturate the marketplace. It's a constant battle to stay on top of the trends that can quickly swing sales each season.

Bearing the harsh reality of the dungaree trade in mind, Koon is planning a slow expansion. He's sinking an additional $3 million in Private Stock's fall 2011 collection, which will expand to 40 bottoms, including 16 variations of jeans, plus an array of cashmere, bamboo, and poplin coats, shirts, and knitwear. In the meantime, his spring collection will make its debut in about 75 boutiques in the U.S. with the hope of eventually landing in trend-setting department stores. "The company, especially in this market, needs to grow organically," says Marchiori. "It will be a long process, but if [Koon] follows his intuition and makes something that is really different and new, he will be able to do it."

While that process might undermine Koon's ultimate goal of becoming a billionaire by the age of 30, he's still preparing himself with the trappings of moguldom. In a stunt that would make even The Donald proud, Koon had his business cards custom made from 18-karat gold. Why this marriage of stationery and bling? Says Koon: "So that nobody would ever forget me." **B**



Koon's business card is made from 18-karat gold



Private Stock's Wyndham Cardigan ($168)

Koon's denims can run up to more than $1,000 per pair

Private Stock's Ice House Woven button-down shirt ($128)

KOON, BUSINESSCARD: PHOTOGRAPHS BY MARTHA CAMARILLO FOR BLOOMBERG BUSINESSWEEK

Etc. The Office Lab

Airport Gate Semiotics

What we do while waiting for our flights ... and what it says about us.

By Tim Murphy

Hello, pilgrim. You say you spent two days after Christmas stuck at an airport gate that smelled like ski socks? At least you weren't lonely. Some 1.2 million travelers were affected over the holidays when East Coast blizzards forced the cancellation of 8,200 flights. (Europe didn't fare much better.)

As a result, a lot of travelers bided their time in airport waiting areas, which the industry refers to as "hold rooms." These are designed to be neutral nonspaces. "You've gone through the stress of security and put yourself back together. Now you're simply waiting in this unusual little lull," says Bill Hooper, a principal at Gensler, the architectural firm that designed JetBlue's new Terminal 5 at John F. Kennedy International Airport in New York.

When the little lull stretches into multiple hours, however, the pilgrims get restless. That's what *Bloomberg Businessweek* discovered while observing 250 people waiting in Paris' Charles De Gaulle, Montreal's Pierre Elliott Trudeau, and New York City's LaGuardia airports earlier this winter. What follows is a typology of airport behavior as analyzed by an expert panel: Patti Wood, author of *Success Signals: A Guide to Reading Body Language*; Jason Barger, author of *Step Back from the Baggage Claim: Change the World, Start at the Airport*; and David Givens, author of *Your Body at Work: A Guide to Sight-Reading the Body Language of Business, Bosses and Boardrooms.*

Next time, don't shovel down that Cinnabon so quickly—unless you want everyone to know that flying stresses you out. Ⓑ

4% *(of people observed)*

Luggage Riflers

Some travelers constantly repack their bags for fear that they lost something—or that something bad is going to happen. "They're controlling the one thing they can control," Barger says. Wood: "It's almost obsessive behavior."

10%

CNN Segment Chortlers

Travelers who laugh along with lighthearted segments on TV monitors want to connect with fellow travelers. "People don't usually laugh when they're alone," says Givens. "When you're waiting together, you share a bond."



4%

Twitchers and Touchers

Chronic foot and knee bobbers and face touchers often "have a hard time being right in the moment," notes Barger. Meanwhile, Wood explains, "It can also mean, 'I want to move on, get someplace.'"

2%

Fortress Builders

Bag pilers give off different signals depending on the configuration of the luggage. "Bags in front mean protection from attack," Wood says. "Bags to either side say, 'I want privacy.' It's prevalent among business travelers."

Other Notable Yet Less Common Airport Gate Behaviors ▸ SOCK CHANGER / Barger: "He must be on a

they're being perceived as important."▸ CELL PHONE YAKKER / Givens: "Staying connected when you're among strangers

17%

Food Stuffers

"When we don't have our bearings, we do things that make us feel good," says Barger, explaining why some travelers eat in a squirrel-like manner. Givens: "This could be your last flight. You owe yourself McDonald's."

3%

Manifest Destiny Snoozers

When people sleep by stretching out across several seats, Wood says, their body language indicates "they have a right to take up more space." Barger notes: "They're making others adjust to what they think is appropriate."

11%

The Existentialists

"The human face at rest tends to look unfriendly," Givens says, and travelers staring into the distance often look disgruntled. "It's like a hospital waiting room," Wood says. "We feel like we're in purgatory."



20%

The Wired Neurotic

"We feel like we have to be working every moment or we're not valuable," says Wood about those who won't detach from their devices. Adds Givens: "You'll see this burst of letting people know where you are."

18%

Tabloid Readers

People who hold gossip magazines up to their faces are looking for an escape. "It changes our brain patterning and creates a subtle high," says Wood. "You rarely see people reading something educational."

8%

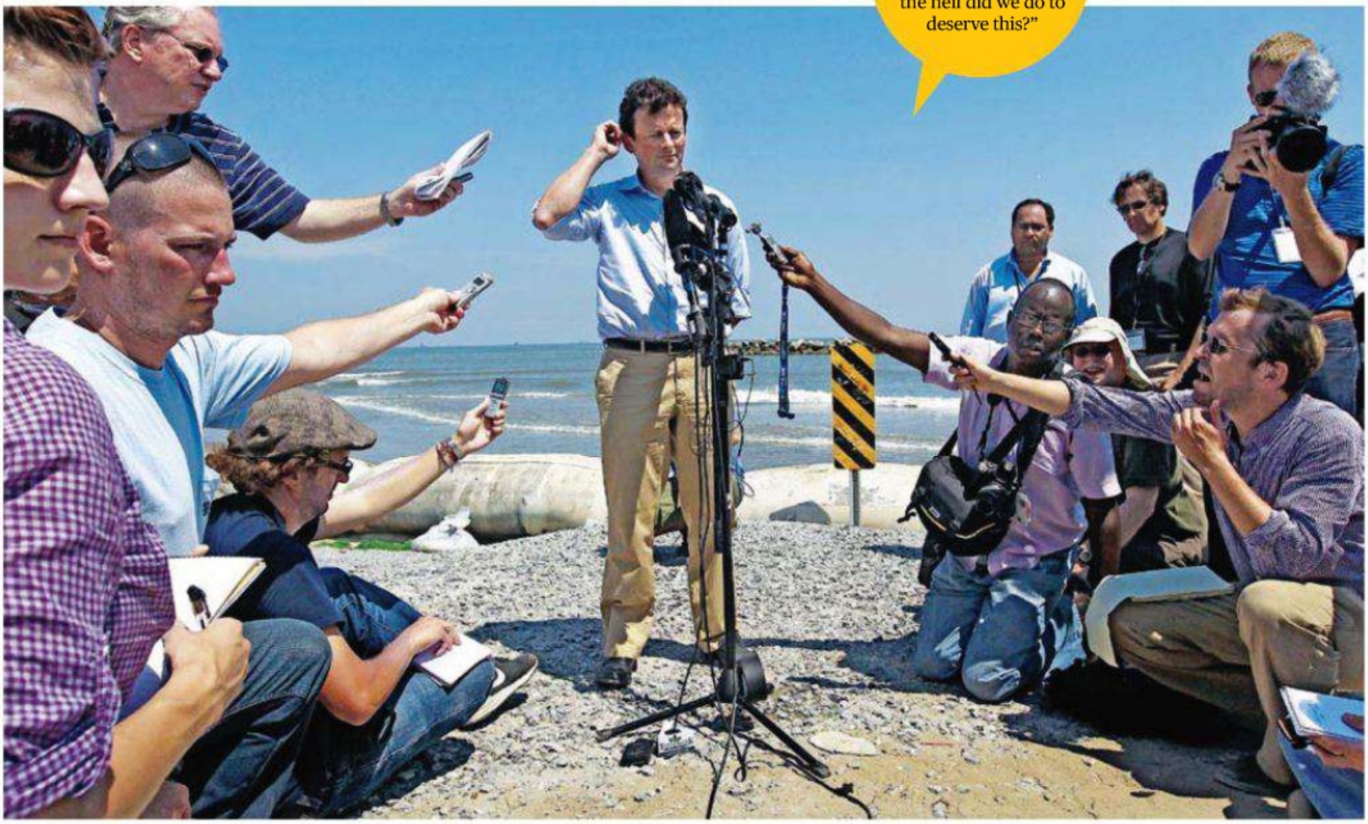
Chair Hoarders

An old-fashioned demarcation of turf. "If you put your bag on the next seat, you're assured that a 350-pound person isn't going to plop down and invade your space," Givens says. "It's holding on to territory."

serious journey." ▶ GATE PACERS / Barger: "They're telling others, 'Don't come talk to me.'" ▶ SKYPER / Givens: "They know is comforting." ▶ SIPPY-CUP-SIPPING GROWN-UP / Barger: "I don't know what to say. There's probably a lot going on."

ILLUSTRATION BY ANDREW BANNECKER

Embattled former CEO Tony Hayward once asked BP executives, "What the hell did we do to deserve this?"



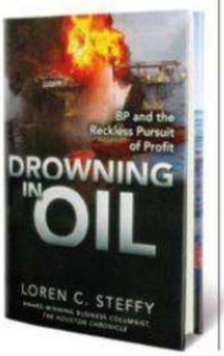
There Will Be Blood

The spill of BP books has begun—just as the disaster begins to recede. *By Paul M. Barrett*

Only five months have passed since BP plugged the gusher in the Gulf of Mexico, yet the oil spill already has a time-warp feel to it. The whole 24/7 spill-cam experience, which lasted for 107 days, seems like ancient history partly because preliminary studies are showing far less environmental damage than had been predicted last spring. The joy of learning about oil-gobbling bacteria has dulled our recollection of petroleum-drenched pelicans.

Corporate obfuscation has also muddled the memory—as it's supposed to. After Robert Dudley replaced Chief Executive Officer Tony Hayward, BP reshuffled management and created a new worldwide safety division. These actions seemed like a welcome admission that BP had made serious mistakes that required radical reform of its culture. Or not. Said Dudley: "I wouldn't describe it as an admission of anything."

Drowning in Oil: BP and the Reckless Pursuit of Profit
By Loren C. Steffy
McGRAW-HILL
286 pp, $27



Months later, fingers are still pointing furiously. BP, the owner of the well, blames Halliburton, which poured the concrete—and vice versa. Transocean, operator of the doomed Deepwater Horizon rig on which 11 people died, surely bears some responsibility, but no one has clarified what that might be. Protracted litigation, including a civil suit filed last month by the Justice Dept., may shed light on culpability. More likely, though, it will lead to a series of gazillion-dollar settlements without concessions of wrongdoing.

Into these murky waters plunge the quick-turnaround book authors. Among the notable early releases are *In Deep Water* by Peter Lehner, executive director of the Natural Resources Defense Council, and *Blowout in the Gulf* by academics William R. Freudenburg and Robert Gramling. More volumes are on the way, including *In Too Deep* by Bloomberg News reporters Stanley Reed and Alison Fitzgerald. One of the first entries in this oeuvre is *Drowning in Oil* by Loren C. Steffy, a columnist for *The Houston Chronicle*.

Unless you spent 2010 on another planet, *Drowning in Oil* will offer little that's new. Yet it has value as a well-researched, clearly stated reminder of



what actually happened. Steffy demonstrates that the rush to pump oil—at bottom, a financial issue—contributed heavily to the disaster, as did overconfidence in technology.

BP became a reckless global oil juggernaut under the leadership of Lord John Browne, Steffy writes. The dashing CEO known for pushing the green-tinged "Beyond Petroleum" marketing campaign also emphasized relentless cost-cutting that translated into postponement of safety improvements and routine maintenance. During Browne's tenure, BP accumulated more than its share of minor oil spills, refinery mishaps, and worker fatalities. The worst was a conflagration, in March 2005, at the company's Texas City (Tex.) refinery, 40 miles south of Houston, in which 15 employees died. BP blamed low-level workers for the blaze. Federal investigators dug deeper and found that a portable meeting room became a death trap because it had been improperly placed in proximity to dangerous equipment. Safety monitors weren't functioning, and alarm bells failed to sound.

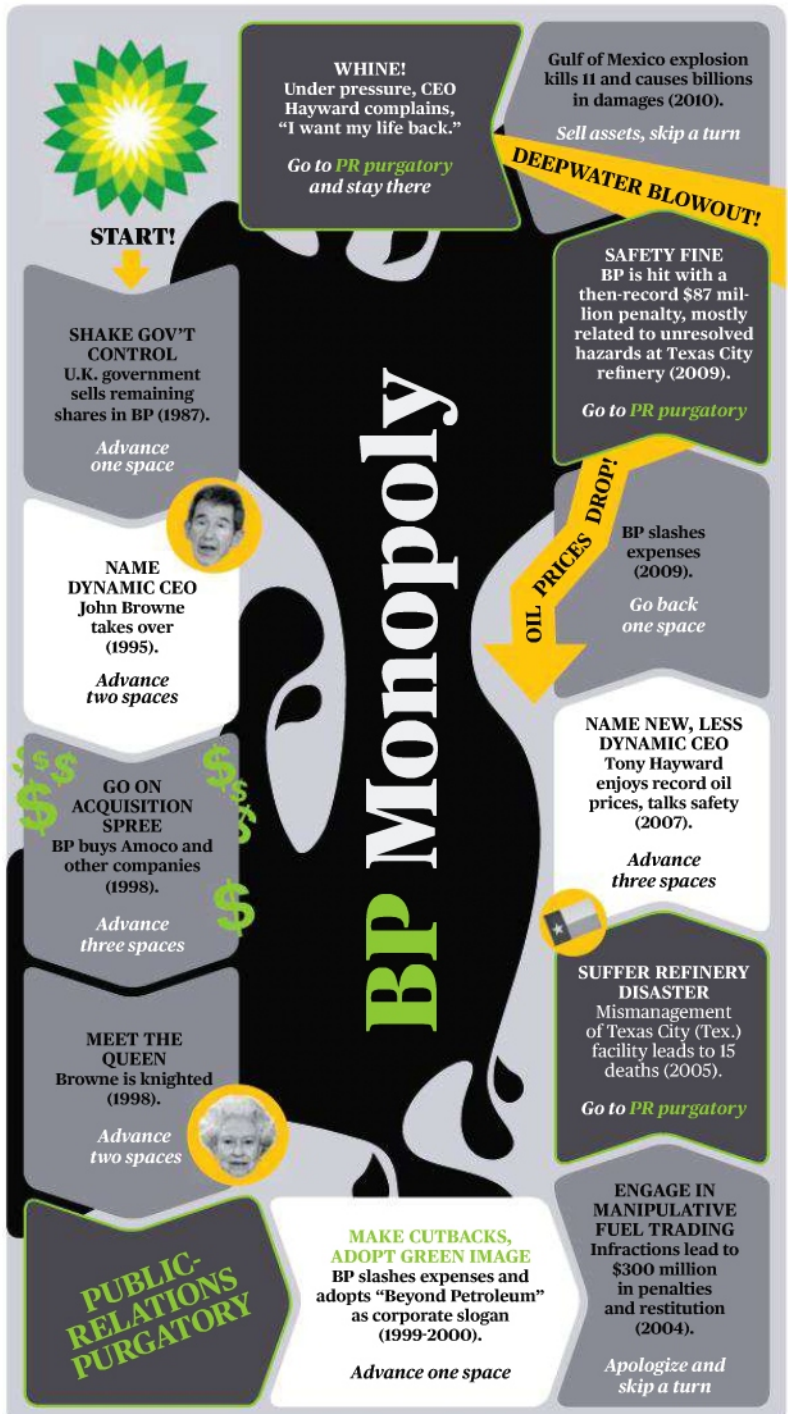
When Browne resigned in 2007, Tony Hayward ascended to CEO. A geologist who resembles the actor Colin Firth, Hayward talked a big game about improving safety, but his inaction spoke louder. Steffy, a former reporter for Bloomberg News, explains that the company's offshore operations were characterized by a perpetual race to get oil flowing as quickly as possible. Hayward and other executives assumed that the absence of a deepwater calamity in the Gulf meant there never could be one. That fallacy—believing an unlikely event will not occur because it hasn't—may remind discerning readers of the financial industry's hubris about the unlikelihood of a nationwide real estate bust.

As the BP project began running behind, costing the company $1.5 million a day, Steffy shows that managers and line workers made elementary mistakes under pressure. They used seawater instead of heavy drilling mud to fill the well. They failed to pay close attention to tests showing that the well was unstable. The blowout preventer, a massive device meant to shear through pipe and cut off an unintended release of oil, did not do its job, for reasons that still haven't been determined. The cost of mopping up will total tens of billions of dollars.

Eventually, we'll know why the blowout preventer stalled at the crucial moment. Other authors, whose publishers gave them more time to let investigations play out, may offer more complete accounts of the debacle. In the meantime, by narrating what is known now and providing crucial corporate context, Steffy has cut through the clutter to remind us of some of the basic reasons all that oil got into the Gulf. Ⓑ

A Game of Chance

Can an oil company climb to dominance without risking the largest environmental disaster in history? BP rolled the dice...



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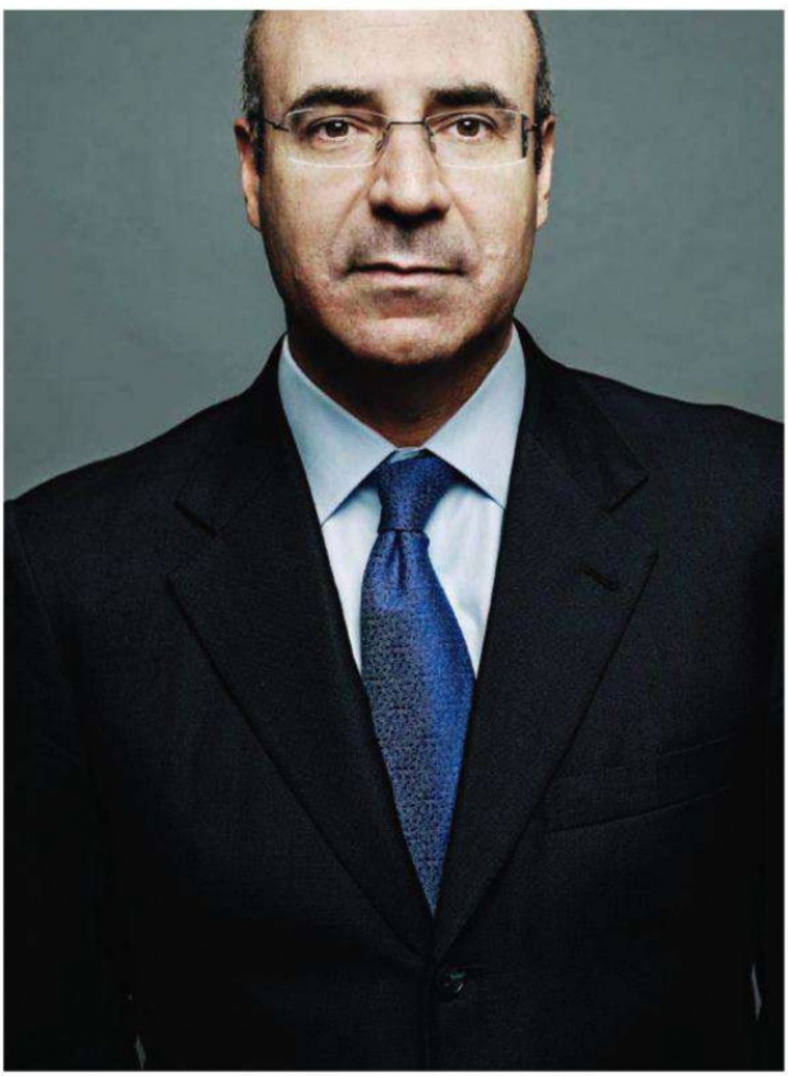
OPPOSITE PAGE: JOHN MOORE/GETTY IMAGES; THIS PAGE: HAYWARD: ROGER L. WOLLENBERG/UPI/NEWSCOM; FIRTH: FRANCOIS DURAND/GETTY IMAGES; BROWNE: ODD ANDERSEN/AFP/GETTY IMAGES; QUEEN: JOHN STILLWELL/WPA POOL/GETTY IMAGES; FLAG: THOMAS NORTHCUT/GETTY IMAGES

Etc. Hard Choices

William Browder

"When Russia defaulted on its debt in 1998, the oligarchs started misbehaving. Our fund went from $1 billion to $120 million"

The Hermitage Capital founder and former Putin ally on how exposing corruption in Russia affected his investment strategy—and worldview



My grandfather was the general secretary of the American Communist Party. And as I was finishing business school in 1989, I had a romantic attraction to the Soviet Union as it was opening for business. As an investment banker in 1992, I went to the Russian town of Murmansk to advise the managers of a state-owned fleet of 100 ships. Each ship cost $20 million, but the managers were being offered the chance to buy 51 percent of the entire fleet for $2.5 million. I realized that to make money in Russia, you had to invest directly in assets that were being privatized. In 1996, I moved to Moscow and set up the Hermitage Fund, which became the largest foreign investment fund in the country.

I figured that if I was buying at a heavy discount—and playing it out until Russia became a civilized country—I could eventually make 100 times my money. However, when Russia defaulted on its debt in 1998, the oligarchs started misbehaving. Our fund went from $1 billion to $120 million. I became a shareholder activist at companies like Gazprom, where we exposed that billions in assets had been stripped. We built the fund up to $4.5 billion.

However, my approach was hugely disliked: In late 2005, I was stopped in the Moscow airport after a business trip and denied reentry. The Russian police then raided my offices and perpetrated a fraudulent tax refund of $230 million. A lawyer we hired to stop the fraud, Sergei Magnitsky, was arrested and died in a Moscow prison in 2009. Not one of the Russian officials involved in his death has been arrested. Many have been promoted and given state honors. I'm lobbying governments to sanction these people and freeze their assets. I'm getting death threats, but I won't stop until we get justice.

I now live in London and am a global investor. My relationship with the world used to be about how much money I made or lost. Now it's more about humanity. Russia is becoming criminalized at an exponential rate. I wish I had not gone there. Ⓑ
—As told to Diane Brady

PHOTOGRAPH BY CHRIS FLOYD FOR BLOOMBERG BUSINESSWEEK



How would you use our technology to make a better world?

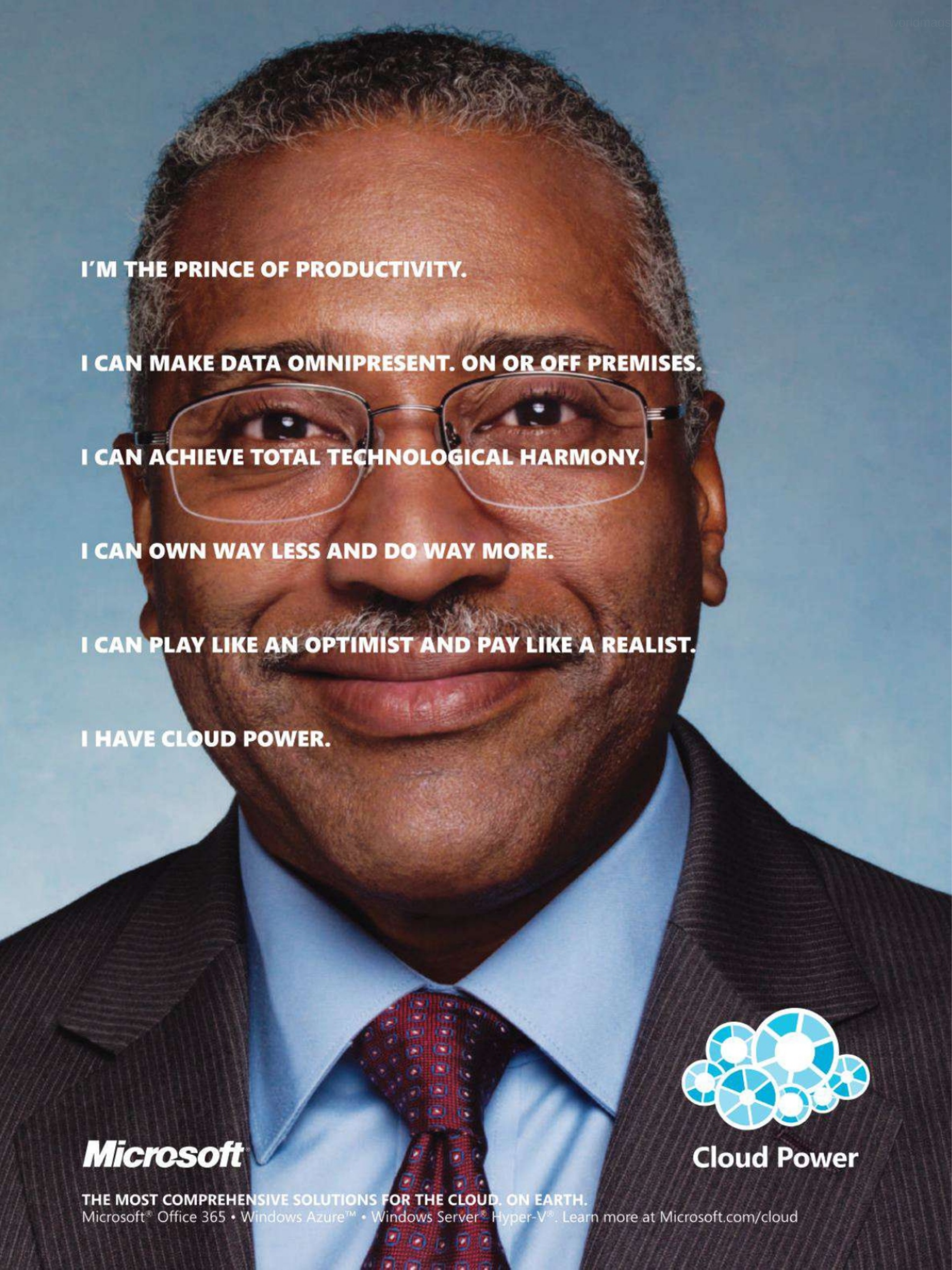
Learn how to share your ideas at toyota.com/ideasforgood

Five winners may have their ideas brought to life and get their pick of a new Prius, Highlander Hybrid or Venza.



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